U. S. FEDERAL REVENUE SHARING: BLUEPRINT FOR LOCAL TAX RELIEF OR INCREASED TAX BURDEN?

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CHAPTER I

INTRODUCTION

Definition of the Problem Area

The state and local governments of the United States bear the brunt of many difficult domestic problems such as education, health, and welfare. The costs of providing these services tend, in many cases, to exceed the economic growth of the communities. Hence, the ability to meet these increasing demands has steadily deteriorated in many areas, most notably the large cities. This has been particularly true during the last decade. The dramatic increase in spending at the state and local levels has come about in response to a number of developments: general population growth, increases in size of our cities and the accompanying need for more social and economic services, rising inflation, and the increasing tendency for people to expect the government to solve more problems for the individual. Adding further to the financial problems of many communities has been the flight of middle and high income people from cities to the suburbs, leaving cities with the heavy burden of providing services to large numbers of people with low incomes who are able to pay only a small share of the cost of government services.

State and local revenues, based primarily on sales and property taxes, often do not keep pace with national economic growth.[1]

The pressing financial situation of many of the state and local governments, particularly the large cities, provides part of the backdrop that led the Nixon Administration to devote its efforts toward some type of Federal assistance to the state and local communities. In his address to the Nation on domestic programs on August 8, 1969, President Nixon stressed the necessity of implementing a revenue sharing system as soon as possible. In a series of successive moves, the Nixon Administration and legislative supporters introduced revenue sharing bills that finally saw passage on October 20, 1972, of the State and Local Fiscal Assistance Act of 1972.

Supporters of revenue sharing legislation assert that state and local governments in general are experiencing a fiscal crisis that can be alleviated only by funds from the Federal Government, and that the Act of 1972 will not only relieve this crisis, but will also reduce the pressures for increased property taxes, put money where the need is greatest, move money and power closer to the people, and combine resources and responsibilities at appropriate levels of government.[2] Opponents, on the other hand, while admitting that some local governments, primarily the large

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[1] H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Finance, U.S. Senate, Report Together with Additional and Minority Views (to Accompany H.R. 14370), p. 9.

[2] U.S. Department of the Treasury. What Revenue Sharing Is All About. (Washington, D.C.: Government Printing Office, 1972), pp. 2-3.

cities, do face a fiscal crisis, deny that state and local governments face a common fiscal crisis and maintain that revenue sharing is a disastrously conceived concept that will do more harm than good. Opponents of revenue sharing also maintain that the system as finally adopted is not designed to aid those governments with the greatest need for assistance.[1]

The Research Question

This study is undertaken to examine the provisions of the State and Local Fiscal Assistance Act of 1972, discuss the goals of this act and the premises on which these goals are based, evaluate the conflicting views of the proponents and opponents of revenue sharing, and assess the ramifications of this new system of Federal assistance. The primary research question can then be stated as: "What are the implications of current Federal revenue sharing for future taxation measures by state and local governments?"

To facilitate the development of the topic, the following subsidiary questions will be investigated:

1. What changes in the concept of Federal revenue sharing took place from the time legislation was first introduced in Congress to the time it was enacted into law?
2. What political trade-offs were necessary to achieve passage of revenue sharing legislation?

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[1]H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Ways and Means, U.S. House of Representatives, Report with Supplemental, Additional, and Dissenting Views (to Accompany H.R. 14370), pp. 88-110.

3. What is the present status of the revenue sharing program?
4. How will revenue sharing affect state and local spending?
5. How will revenue sharing affect state and local taxation?

Purpose and Objectives of the Study

The purpose of this study is to determine the effects that revenue sharing will have on the administration of the state and local governments insofar as spending and taxation policies are concerned. This determination will necessitate consideration of the national politics involved in the passage of revenue sharing legislation, factors relating to the computation of funds received by each unit of government, and the expectations of the public as to the permanency of revenue sharing.

Scope of the Study

It was originally intended that this study investigate the ramifications of revenue sharing at both the national and local levels of government, but it soon became apparent that the complexity of the Federal budgetary and taxation processes prohibited the inclusion in a limited study of this nature of the effects of revenue sharing on the national economy. It was decided, therefore, to concentrate on the state and local governments, primarily the latter, inasmuch as these units of govern-

ments were to be the recipients of the benefits of revenue sharing. The role of the Federal government in adopting revenue sharing funds, and the amount of money involved are discussed in this study, but there is no attempt to explain how the money is to be raised by the Federal government or determine the possible affects on Federal taxation policies or the national debt.

Methodology

The information for this study was gathered from both primary and secondary sources. Interviews were conducted with officials of several Federal agencies, U.S. Representative Ella T. Grasso of Connecticut, and with mayors, city managers, and other officials of city, town, and county governments in several states. No written questionnaire was developed for mailing purposes, but questions appropriate to each interview were prepared in advance of the scheduled interview for use therein. Information obtained by interview is used in various sections of this paper, but inasmuch as most of the interviews were conducted with local executive officials to ascertain their intended use of revenue sharing funds, most of this information is included in Chapter VI and Appendix II.

The remaining information for this study was obtained from secondary sources and is used in the development of background and technical information. The secondary sources were generally in the form of official publications or documents of a public nature.

The analysis of the data gathered was inductive in nature and the conclusions were reached using this manner of reasoning. There was no attempt to arrive at conclusions using statistical methods. Much of the information obtained by interview was tentative in nature and in any event was not easily adaptable to statistical or computer applications.

Limitations

Revenue sharing as adopted by the Act of 1972 is a very new concept. The first checks under this system had just been distributed by the Treasury Department at the time interviews were conducted and other sources investigated. Many units of government have not yet decided how their funds are to be employed and many questions remain concerning the proper use of funds, monitoring of the system, and the future of revenue sharing. Therefore, the conclusions arrived at in this study are based on a very limited experience under the new revenue sharing system. This system under the 1972 legislation has a scheduled life of five years, so the possibility exists that the eventual effects of revenue sharing will not be the same as presently anticipated.[1]

As previously mentioned, the conclusions of this study are not based on statistical methods, but rather on inductive reasoning, employing information from primary and secondary sources.

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[1] State and Local Fiscal Assistance Act of 1972, Sec. 105, 86 Stat. 919 (1972).

Organization

This study begins with a background survey of the revenue sharing concept and traces the evolution of Federal revenue sharing as a solution to the perceived problems of state and local governments. The goals of revenue sharing are then discussed, recognizing that both political and economic considerations are involved. The provisions of the State and Local Fiscal Assistance Act of 1972 are discussed in some detail, with prominence accorded the formulas for computing the funds for each state and locality. The component factors of these formulas are examined in order to identify the incentives represented by the Act of 1972 and to clarify some of the political goals of the legislation.

The purposes for which revenue sharing funds will be used are considered next, using information from both primary and secondary sources, after which alternatives to revenue sharing are evaluated. Finally, the ramifications of revenue sharing, both the desirable and undesirable features, are assessed and conclusions drawn concerning its impact on the expenditure and taxation policies of state and local governments.

CHAPTER II

THE GOALS OF REVENUE SHARING

General

Revenue sharing has often been stressed as a policy instrument of great versatility by its proponents and has been presented as a program with many different simultaneous objectives. In his revenue sharing message to Congress on August 13, 1969, President Nixon stated:

> Our ultimate purposes are many: To restore to the States their proper rights and roles in the Federal system with a new emphasis on and help for local responsiveness; to provide both the encouragement and the necessary resources for local and State officials to exercise leadership in solving their own problems; to narrow the distance between people and the government agencies dealing with their problems; to restore strength and vigor to local and State governments; to shift the balance of political power away from Washington and back to the country and the people.[1]

Revenue sharing as envisioned by President Nixon is the keystone to his philosophy of "New Federalism" under which power and influence would flow to the state and local governments, reversing the trend of the past few decades. As the President views the situation, it was the flow of money to Washington following the

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[1] Legislative Reference Service. Library of Congress. Resolved: That the Federal Government Should Grant Annually A specific Percentage of Its Income Tax Revenue to the State Governments: A Collection of Excerpts Relating to the Intercollegiate Debate Topic, 1969-1970, (Document No. 91-158). Washington, D.C.: Government Printing Office, 1970, p. 4.

adoption of the personal income tax early in this century that created the concentration of power and authority in Washington, and only a reverse flow of money can create a corresponding reverse flow of power and authority.[1]

The key words in the President's message to Congress consist of the phrase, "Our ultimate purposes are many." Some of the purposes have been described in detail and appear to be fairly straightforward. Other purposes seem to be referred to in a more oblique manner. Revenue sharing is definitely much more than an economic measure designed to assist lower echelon governments. Some of the more detailed goals and purposes of revenue sharing are discussed below.

Fiscal Assistance to State and Local Governments

Perhaps the most immediate goal of revenue sharing is to help relieve the fiscal pressures on the state and local governments.[2] This goal is both quantitative and qualitative in nature: quantitative in the sense that Federal funds are to be added to the limited local resources, and qualitative in the sense that improvements in the quality of local services are to be realized, especially in the poorer states, and that local initiative and responsibility are to be stimulated as part of the national interest in revitalizing state and local government.

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[1] Ibid., p. 2.

[2] Ibid., p. 21.

Revitalization of State and Local Government

In addition to the benefits of immediate cash, the vitality, efficiency, and fiscal independence of state and local governments are to be enhanced.[1] This goal is actually a re-expression of the traditional American faith in pluralism, decentralization, and diversity. Implicit in this goal is that there is enough money at the Federal level to finance our national programs, but there is not enough wisdom to administer them at that level. Therefore, the states and localities are to be relied upon to carry out the centrally financed programs. This revitalization is to be brought about by providing new financial elbow-room, free of political penalties that would accompany an increase of local taxes; by nourishing the purely local services and building a staff and structure to carry them out effectively; and by enabling the economically weaker states to provide the same scope and quality of services as the wealthier states, without imposing unreasonable burdens on their citizens.[2]

Movement of Money and Power Closer to the People

President Nixon has repeatedly emphasized the view that the government closest to the people, i.e., state and local government, is best able to provide the services that directly affect most of the people. Revenue sharing, therefore, is to provide the flow of both funds and power to the local level

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[1]*Ibid.*, p. 21.

[2]*Ibid.*, pp. 26-27.

for this purpose. Narrowing the distance between people and the government is a recurring theme of the "New Federalism."

Redistribution of Income

Redistribution of income is not one of the goals of revenue sharing to which the President has given emphasis, but the structure of the legislation leaves no doubt that this is a major goal of revenue sharing as ultimately adopted. Though difficult to pinpoint, there is a good deal of evidence that the redistribution aspect of the bill resulted primarily from Congressional manipulation.

Stimulation of State and Local Tax Efforts

It has long been recognized by even the most ardent proponents of revenue sharing that many state and local governments have not employed their tax resources to the fullest possible extent and that many of these units of government are experiencing fiscal difficulties primarily because they have failed to institute the necessary taxation measures.[1] For this reason all the various revenue sharing proposals, including the President's original proposal and the final Act of 1972, have given great emphasis to rewarding those governments that maintain or expand their own taxation efforts. This emphasis has taken the form of a "general tax effort" factor used in the revenue sharing formulas

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[1] H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Ways and Means, U.S. House of Representatives, Report with Supplemental, Additional, and Dissenting Views (to Accompany H.R. 14370), p. 92.

for distribution of funds.[1] This will be discussed in more detail in Chapter V.

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[1] State and Local Fiscal Assistance Act of 1972. Sec. 109, 86 Stat. 919 (1972).

CHAPTER III

BACKGROUND SURVEY OF THE REVENUE SHARING CONCEPT

General

The general concept of revenue sharing took shape in America as far back as 1805 when President Jefferson in his second inaugural address urged that Federal revenue be used among the states for canals, rivers, roads, arts, education and other great objects within each state.[1] However, this concept received little serious consideration for another century and a half. Though the Federal Government long ago established a system of grants-in-aid to states, funds transferred to the states under this program were allocated for specific projects and there was no attempt to use the grants-in-aid system as a form of revenue sharing over which the states could exercise control. In the 1950's and 1960's a resurgence of interest in a system of Federal revenue sharing arose amidst both academic and political leaders. No concrete results in the form of legislation took place during these two decades, but the interest in such a plan was sustained, and gradually more influential people perceived the need for some form of revenue sharing as essential

[1]Executive Office of the President. The Domestic Council. The History of Revenue Sharing. Washington, D.C.: Government Printing Office, 1971, p. 1.

to national and local government interests.

America has changed radically during the past few decades, particularly since World War II. The economic, social, and political developments of this period have greatly enhanced the fiscal position of the national government and have resulted in the flow of vast political power to the Federal government.[1] At the same time, the forces that brought about these changes have contributed to the plight of the state and local governments. The net result has been the creation of what has been called "the fiscal mis-match."[2] In other words, there has been a reversal in the fiscal relationships between the Federal government and the state and local governments. For example, in 1930 state and local governments collected more taxes than the Federal government; today, however, the Federal government collects two-thirds of all taxes. Prior to 1940, the Federal government devoted over 80 percent of its budget to domestic purposes, but today only 44 percent of the Federal budget goes for domestic purposes.[3] One factor has remained constant while this reversal of roles took place: the American people still look to the state and local governments for social and educational services.

While political power and funds generated by taxation have become concentrated at the national level, drastic changes in

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[1]National League of Cities - U.S. Conference of Mayors. Support Revenue Sharing. Washington, D.C., 1972, p. 14.

[2]Ibid.

[3]Revenue Sharing Advisory Service, Inc. Why Revenue Sharing?. Washington, D.C., 1972, p. 7.

patterns of living have rapidly increased the urbanization of American society, resulting in the demand for more extensive social, welfare, and educational services at the local level. The continuation of the Industrial Revolution, particularly the rapid industrialization of agriculture, created a rural-to-urban migration that has resulted in an increasing concentration of unskilled workers in the urban centers, which, in turn, has caused middle and upper income groups to congregate in the suburbs.[1] Other factors have aggravated this polarization of the poor, unskilled workers in the core cities and the middle and upper income groups in the suburbs. Fragmentation of the national welfare system allowed many states to pay only a fraction of the relief that was being paid in other states, thus creating a migration from the rural South to the industrialized cities of the North. Federal Housing Authority (FHA) policies contributed to urban sprawl and the flight to the suburbs of the middle and upper income groups by subsidizing more than ten times as many units of housing in the suburbs than in the inner city. The national highway program further stimulated the suburban exodus by the construction of endless freeway systems while ignoring the need for urban mass transit. Therefore, national policies have contributed to the steady deterioration of the nation's cities.[2] The demand for services in the cities remains high, but the populations thereof are able to pay only a small share of the expenses.

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[1] Revenue Sharing Advisory Service, Inc. Why Revenue Sharing?, Washington, D.C., 1972, p. 6.

[2] Ibid.

It was the plight of the large cities that sparked the drive for a system of Federal revenue sharing, though as we shall see later, the system as ultimately adopted does not give particular emphasis to solving the cities' fiscal problems. In presenting his revenue sharing proposal to Congress, President Nixon stated:

> The growing fiscal crisis... in our states and communities is the result in large measure of a fiscal mismatch; needs grow fastest at one level while the revenues grow fastest at the other. This fiscal mismatch is accompanied, in turn, by an "efficiency mismatch"; taxes are collected most efficiently by the highly centralized Federal tax system while public funds are often spent most efficiently when decisions are made by state and local authorities. What is needed, then, is a program under which we can enjoy the best of both worlds, a program that will combine the efficiencies decentralized expenditure. What is needed, in short, is a program for sharing Federal tax revenues with state and local governments.[1]

Sources of Revenue of State and Local Governments

State and local governments rely heavily on property and sales taxes for revenues, and for this reason additional tax revenues have recently become increasingly difficult to obtain. Inasmuch as these revenue sources do not increase rapidly as income levels rise, revenue increases must be obtained through rate increases, a politically distasteful and dangerous course of action at the lower levels of government.

For many core cities the financial problems are particularly acute. The movement of middle income and high income

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[1] Executive Office of the President. The Domestic Council. The History of Revenue Sharing. Washington, D.C.: Government Printing Office, 1971, p. 16.

people to the suburbs has resulted in a dwindling tax base for the cities. Another factor aggravating this situation is that some states and localities have not made effective use of the revenue resources available to them. There are substantial variations in the tax effort made by the various states and localities.

In 1970 state and local governments derived about 74 percent of their total tax revenue from property and sales taxes--sources whose yields rise only about proportionately with increases in income levels. In contrast, state and local income taxes--the taxes whose yields rise relatively rapidly as income levels increase--accounted for only about 17 percent of their total tax revenue.[1]

Local governments are much more restricted in the taxation measures available to them than are the state governments. Even with heavy sales taxes and local property taxes, local governments in some cases are not able to provide the services expected by the communities. This is particularly true in the large cities. State governments, on the other hand, are experiencing surplus budgets at present, and many could increase their revenues even more through more effective use of the state income tax, etc.[2]

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[1]H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Ways and Means, U.S. House of Representatives, Report with Supplemental, Additional, and Dissenting Views (to Accompany H.R. 14370), p. 5.

[2]"The Fiscal Forecast Is Fine for the States," Business Week, February 17, 1973, p. 68.

Since some local governments clearly are in need of additional sources of revenues, and since the states are in a position to raise these revenues, it seems incumbent upon the state governments to assist the local governments, rather than expecting the Federal government to do so. In any event, it is clear that Federal revenue sharing is not the only remaining solution to the problems of the big cities.

Fiscal Situation of State and Local Governments

It is difficult to generalize about the fiscal situation of state and local governments, inasmuch as there are almost 39,000 units of local government in addition to the 50 state governments.[1] The governments with the severest fiscal situation, however, are the large cities. The migration of low income groups to the cities, the departure of the higher income groups therefrom, and the limited taxation measures available to the cities have already been discussed. Most state and local governments, exclusive of the large cities, however, are not experiencing fiscal difficulties that cannot be solved by taking reasonable measures within their authority.

As a matter of fact, most state governments have operated with a small budgetary balance in the past few years. There were 17 states that experienced a deficit in 1968, 8 in 1969, and 14 in 1970. Furthermore, most of those with deficits were only

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[1] U.S. Department of the Treasury. What Revenue Sharing Is All About. Washington, D.C.: Government Printing Office, 1972, p. 1.

slightly in the red. In the aggregate, state governments in 1970 received revenues of $130.8 billion and expended $131.3 billion, for a deficit of only a half billion dollars.[1] Compared to the Federal deficit, a half billion dollar deficit in the state governments is insignificant, even taking into consideration the difference in levels of receipts and expenditures.

Several states are realizing a very substantial surplus in their budgets. Florida, for example, a state that has no personal income tax and a modest sales tax of 4 percent, has a projected surplus of $300 million for the 1973 fiscal year.[2] This surplus results primarily from revenue from a recently adopted corporate income tax and $38 million to be received from Federal revenue sharing.[3] Clearly this is a state that can do quite nicely without the revenue sharing funds.

Maryland's Governor Marvin Mandel recently asked the state legislature for a $2.467 billion budget that represents a 13.7 percent rise over the current budget and projects a $39,588 surplus with no tax increases to be imposed.[4] This represents a razor-thin surplus, to be sure, but it nevertheless demonstrates the ability of that state to meet its obligations without experiencing a deficit. In general there is no reason to doubt that

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[1] U.S. Bureau of the Census, Statistical Abstract of the United States: 1970-1972, Washington, D.C.

[2] The Tampa Tribune, December 18, 1972, p. 1, Col. 6-8.

[3] Ibid.

[4] The Washington Star-News, January 17, 1973, p. 1 Col. 5-7.

state governments can continue to carry out their responsibilities within the revenue generating measures available to them.

In contrast to the relative well being of the states, 13 of the 25 largest cities experienced deficits in 1967, 14 in 1968, 15 in 1969, and 17 in 1970.[1] The large cities, therefore, are the units of government that are experiencing the most severe fiscal difficulties. Their tax base is limited, the demand for services ever increasing, and their ability to finance budgetary deficits restricted.

Evolution of Federal Revenue Sharing

The social and economic conditions contributing to the fiscal difficulties of the large cities have been mentioned. This section will discuss some of the political history of revenue sharing concepts and the major Congressional hurdles that were surmounted before passage of the 1972 Act could be achieved. Chapter IV will deal with the various revenue sharing bills that were introduced in Congress and trace the political process that ultimately produced the Revenue Sharing Act of 1972.

Though the concept of some type of sharing of Federal revenues by the national government with state and local governments can be traced back to Jefferson's days, the first revenue sharing bill was introduced in 1958 by Congressman Melvin Laird

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[1]U.S. Bureau of the Census, Statistical Abstract of the United States: 1969-1972, Washington, D.C.

of Wisconsin.[1] There was little support for this idea at that time and the bill never reached the floor of the House of Representatives.

In 1960 economist Walter W. Heller of the University of Minnesota developed the "Heller Plan" under which a system of revenue sharing would be used to channel funds to state governments.[2] The states in turn would develop a plan for assisting the cities, towns, and counties. This plan did not attract a great deal of attention at first, but as Chairman of the Council of Economic Advisors during the Kennedy-Johnson Administration (1961-1964), Mr. Heller advocated revenue sharing within high policy circles of government.[3] In 1964 President Johnson instructed economist Joseph A. Pechman to prepare a report on revenue sharing. The contents of this report were never publicized, the President declining to release it.[4]

Support for revenue sharing continued to gather. In 1965 The Ripon Society, a liberal Republican group, endorsed the concept of revenue sharing, and during the 90th Congress (1967-1968) over 100 bills were introduced proposing more than 30

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[1] Revenue Sharing Advisory Service, Inc., Revenue Sharing Bulletin, November 1972, Vol. 1, No. 1, Washington, D.C., p. 1.

[2] Executive Office of the President. The Domestic Council. The History of Revenue Sharing. Washington, D.C.: Government Printing Office, 1971, p. 2.

[3] Ibid.

[4] Revenue Sharing Advisory Service, Inc., Revenue Sharing Bulletin, November 1972, Vol. 1, No. 1, Washington, D.C., p. 1.

different types of revenue sharing programs.[1] Again, none of these bills ever reached the House floor, but it became apparent that some form of revenue sharing was inevitable within the next few years.

Seizing the opportunity of the times, national associations of state, county, and city officials adopted policy positions favoring enactment of a revenue sharing program. In the 1968 election campaign both Republicans and Democrats included revenue sharing planks in their platforms and both presidential candidates publicly supported revenue sharing.[2]

Following his election to the Presidency, Mr. Nixon moved quickly to implement his ideas of the "New Federalism," revenue sharing being central to his concept of returning both money and authority to the lower levels of government. In the spring of 1969, President Nixon and state and local government officials announced agreement on the basic provisions of a revenue sharing program, and on August 8, 1969, the President outlined his program in a nation-wide television address. His stated purpose was to relieve state and local fiscal crises, reduce pressure for increased property taxes, put money where the need is greatest, move money and power closer to the people, and combine resources and responsibilities at appropriate levels of government.

At this particular point, there was no enthusiasm at all for revenue sharing in the crucially important House Ways and

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[1] Ibid., p. 7.

[2] Executive Office of the President. The Domestic Council. The History of Revenue Sharing. Washington, D.C.: Government Printing Office, 1971, p. 2.

Means Committee chaired by the powerful Wilbur Mills of Arkansas.[1] The reaction in the Senate was much more favorable, however. On September 22, 1969, only six weeks after President Nixon's nation-wide address, the Senate Subcommittee on Intergovernmental Relations, chaired by Senator Edmund Muskie of Maine, began hearings on several revenue sharing proposals.[2] Though revenue sharing legislation, like all revenue programs, must originate in the House, Muskie's subcommittee succeeded in focusing public attention on the program.

In the spring of 1970 more than 2,000 state, city and county officials visited their Congressmen to press for support of the revenue sharing program.[3] They publicly urged Congressman Mills to hold committee hearings, but Mr. Mills responded that the committee was busy with many other pieces of legislation having high national priority.[4] Additional pressure was clearly needed if the House Ways and Means Committee was going to be forced to act on revenue sharing proposals.

On June 24, 1970, the President renewed the revenue sharing drive by publicly releasing a memorandum to senior administration officials urging them to espouse the program at every opportunity.[5] In the fall of 1970 state, city, and county officials solicited commitments for the program from over 200

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[1]Revenue Sharing Advisory Service, Inc., Revenue Sharing Bulletin, November 1972, Vol. 1, No. 1, Washington, D.C., p. 7.

[2]*Ibid.* [3]*Ibid.* [4]*Ibid.*

[5]Revenue Sharing Advisory Service, Inc., Revenue Sharing Bulletin, November 1972, Vol. 1, No. 1, Washington, D.C., p. 7.

Congressmen and 59 Senators.[1] In another nation-wide television address in December 1970, President Nixon stated:[2]

> There is nothing I feel more strongly about than the proposal for revenue sharing--the new one that I will be submitting to Congress.

Early in 1971 the Nixon Administration began to push harder for the revenue sharing program. In his State of the Union Message, President Nixon announced a new revenue sharing program budgeted for about $5 billion, ten times more than the Administration's first proposal.[3] Congressman Mills immediately announced his strong opposition to the bill. At this point the U.S. Conference of Mayors began to organize the Legislative Action Committee to focus public attention on critical issues facing American cities and bring pressure on Congress to act. The intense lobbying by the U.S. Conference of Mayors began to bear fruit. The Legislative Action Committee traveled throughout the country in 1971 and 1972 explaining to the media and local citizenry the absolute necessity, as they saw it, for cities to have revenue sharing.[4]

All these forces soon had an affect. On April 22, 1971, Mr. Lawrence O'brien, Chairman of the Democratic National Committee, called a meeting in the Capital of Democratic governors,

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[1] Ibid. [2] Ibid.

[3] "Text of President's Message on Revenue Sharing," Congressional Quarterly, Weekly Report, February 12, 1971, Vol. XXIX, No. 7, p. 392.

[4] Revenue Sharing Advisory Service, Inc., Revenue Sharing Bulletin, November 1972, Vol. 1, No. 1, Washington, D.C., p. 7.

mayors, Senate and House leadership to discuss domestic programs, including revenue sharing, and on May 11, 1971, Chairman Mills announced that the House Ways and Means Committee would hold public hearings on revenue sharing beginning June 2, 1971.[1]

During the hearings in June 1971, before the House Ways and Means Committee, Chairman Mills, while objecting to the Administration's general revenue sharing plan, reluctantly agreed to support a program of his own design to aid state and local governments.[2]

On June 22, 1972, the House of Representatives approved the revenue sharing bill as constructed by Mr. Mills, and on September 12, the Senate passed the bill by a vote of 64 to 20.[3] About a month later both the Senate and the House accepted the Conference Committee's report and on October 20, 1972, President Nixon signed the bill into law.

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[1] Ibid.

[2] Ibid.

[3] "Senate Revenue-Sharing Bill Favors Small, Rural States," Congressional Quarterly, Weekly Report, September 16, 1972, Vol. XXX No 38, p. 2352.

CHAPTER IV

POLITICAL ACCOMODATIONS LEADING TO PASSAGE OF THE REVENUE SHARING ACT

In Chapter III a brief discussion was presented that traced some of the important milestones in the evolution of Federal revenue sharing. It was pointed out that President Nixon had become an early advocate of this plan for assisting the lower level governments, but that no progress was made toward implementation of that goal through the Congressional process until mounting pressure was brought to bear through intense lobbying of organizations representing officials of state, county, and local governments. This chapter will trace the tortuous path of revenue sharing legislation through the various Congressional channels and identify the compromises and adjustments that took place before the bill became law.

President Nixon's Initial Proposal

President Nixon adopted his original revenue sharing plan from a proposal which gained currency during the Johnson Administration. This was the "Heller Plan" referred to in the previous chapter.[1] Mr. Johnson never accepted it publicly, possibly

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[1] Legislative Reference Service. Library of Congress. op. cit., p. 9.

because he saw no opportunity to implement it in the face of the budget deficits brought about by the Vietnam War.

Borrowing generously from the "Heller Plan," Mr. Nixon formulated his original program in early 1969, presenting it to the country in a television address on August 8 of that year. The key provisions of this original plan were:[1]

(1) Earmarking of a small but growing proportion of Federal revenues annually to be returned to state and local governments almost without restrictions on its use.

(2) Allocation among states chiefly according to population but with a factor to reflect and provide incentive for revenue-raising efforts by individual states.

(3) Allocation of about 30 percent of each state's share to its general local governments, according to their revenue-raising efforts.

(4) The expenditure of $500 million in FY '71 and the raising of this amount to approximately $5 billion by FY '76. These sums were geared to anticipated budgetary surpluses.

President Nixon's plan was incorporated in bills (S 2948 and HR 13982) introduced during the 91st Congress, but they met opposition from the two ranking members of the Ways and Means Committee, which handles tax and revenue legislation. Chairman Wilbur D. Mills, joined by John W. Byrnes, the ranking Republican of the Ways and Means Committee, opposed uncontrolled state or local use of funds raised through Federal taxation. Chairman Russell B. Long of the Senate Finance Committee expressed opposition to the plan on the grounds that there were no surplus

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[1] "Revenue Sharing: Bitter Battle Looms in Congress," Congressional Quarterly, Weekly Report, January 29, 1971, Vol. XXIX No. 5, p. 213.

revenues to share. Neither bill was acted upon.[1]

Other Proposals

In the weeks following the President's initial proposal, revenue sharing gained substantial support from state and local officials, the public, and many members of Congress, despite the opposition of key committee leaders. Administration officials led by Murray L. Weidenbaum, Assistant Treasury Secretary for economic policy, met December 6 with state and local officials during a National League of Cities conference in Atlanta, Georgia.[2] At this meeting details for a modified revenue sharing program were worked out, along with an agreement for stepping up the drive for Congressional action on the plan.

In the meantime various Senators and Representatives favoring revenue sharing began to assimilate their own bills, designed in most cases to give maximum advantage to their own constituencies. It is beyond the scope of this study to examine each of these in detail, but the more important ones will be discussed to demonstrate their impact on the bill that ultimately was enacted.

Beginning in late 1969 the Senate Government Operations Subcommittee on Intergovernmental Relations chaired by Senator Edmund S. Muskie held hearings on a revenue sharing bill (S 2483) introduced by Senator Muskie. This bill was drafted by the

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[1] Ibid.

[2] Revenue Sharing Advisory Service, Inc., Revenue Sharing Bulletin, November 1972, Vol. 1, No. 1, Washington, D.C., p. 7.

Advisory Commission on Intergovernmental Relations (ACIR) of which he was a member.[1] This bill never reached the Senate floor, but it is important to note that Senator Muskie, at that time widely regarded as the brightest presidential prospect in the Democratic Party, was an early advocate of some type of revenue sharing. Senator Muskie introduced a quite similar bill (S 1770) in 1971.[2]

Almost simultaneously with the disclosure of the new program worked out by Wiedenbaum on behalf of the Administration, Senator Hubert H. Humphrey and Representative Henry S. Reuss introduced identical revenue sharing bills in the Senate and House, respectively, containing some elements of similarity to and some marked differences from the Administration plan.[3] They announced their proposal in December 1970, whereas Mr. Nixon's official message for his new revenue sharing program was not delivered until February 4, 1971. His revised proposal was introduced in the Senate by Senator Howard H. Baker of Tennessee and in the House by Representative Jackson E. Betts of Ohio as

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[1] U.S. Congress. Senate. Committee on Government Operations. Intergovernmental Revenue Act of 1969 and Related Legislation. Hearings before the Subcommittee on Intergovernmental Relations of the Committee on Government Operations, Senate, on S. 2483 and S. 2048, 91st Cong., 1st sess., 1969, p. 1.

[2] Revenue Sharing Advisory Service, Inc., Revenue Sharing Bulletin, November 1972, Vol. 1, No. 1, Washington, D.C., p. 7.

[3] "Revenue Sharing," Congressional Quarterly, Weekly Report, June 4, 1971, Vol. XXIX, No. 23, p. 1214.

S 680 and HR 4187, respectively.[1] Mr. Humphrey, also a Democratic presidential prospect, wasted no time in placing himself in the forefront of the revenue sharing movement.

At this point, therefore, there were three versions of revenue sharing being pursued by three powerful leaders: the President's revised proposal; Senator Muskie's proposal, based largely on the recommendations of the Advisory Commission on Intergovernmental Relations; and Senator Humphrey's proposal. The major points in common as well as the significant differences of these three proposals will next be considered.

President Nixon's Revised Proposal

Mr. Nixon's new proposal reflected the renewed agreement with state and local leaders nurtured by Mr. Wiedenbaum. Additionally, it represented a quantum jump in the President's commitment to assist state and local governments. The amount of money for the first year of the program was increased tenfold, from an original $500 million to $5 billion.[2] The concept of sharing only surplus revenues was abandoned. Mr. Nixon offered his plan after announcing that he would submit a deficit budget for Fiscal Year 1972.[3] Revenue sharing was treated as any other government

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[1]"Revenue Sharing: Congress Moves Away From Nixon," Congressional Quarterly, Weekly Report, March 12, 1971, Vol. XXIX, No. 11, p. 632.

[2]"Text of President's Message on Revenue Sharing," Congressional Quarterly, Weekly Report, February 12, 1971, Vol. XXIX, No. 7, p. 393.

[3]"Revenue Sharing: Bitter Battle Looms in Congress," Congressional Quarterly, Weekly Report, January 29, 1971, Vol. XXIX, No. 5, p. 213.

expense, although the idea was to make room for it by cutting or eliminating other less urgent proposals.

The new proposal contained a bifurcated concept of general revenue sharing and special revenue sharing. General revenue sharing embodied the distribution of funds ($5 billion per year) to lower level governments relatively free of restrictions. Special revenue sharing involved combining existing Federal aid programs of $10 billion with $1 billion in new funds and using these funds in six broad areas: law enforcement, manpower training, urban community development, rural community development, transportation, and education.[1] A major goal of the special revenue sharing proposal was to consolidate many of the grant-in-aid programs into a few categories designed to achieve specific national objectives, rather than continue the widely dispersed system of programs being financed by Federal grants-in-aid.[2] To complement the special revenue sharing proposal, various bills to incorporate the objectives of the six broad areas mentioned above were introduced.

Special revenue sharing is mentioned here because it was an important corollary to the general revenue sharing proposal submitted in Mr. Nixon's new plan. However, the President's plans for special revenue sharing were never implemented nor enacted into law, so this paper deals only with general revenue sharing which did become law. It is interesting to note that Mr.

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[1] Ibid.

[2] Ibid.

Nixon attempted to overhaul the grant-in-aid program by using general revenue sharing as a vehicle for reorganization. This attempt did not survive the legislative process.

The key provisions of President Nixon's revised general revenue sharing plan were as follows:[1]

(1) The size of the appropriation each year would be a designated percentage of the nation's taxable personal income, the base on which individual Federal income taxes are levied. The fund would therefore grow in a steady and predictable manner with the growing tax base, enabling state and local governments to plan for the future.

(2) The specific appropriation level recommended was 1.3 percent of taxable personal income. At this level approximately $5 billion would be distributed during the first full year of revenue sharing. It was anticipated that this sum would rise to about $10 billion by 1980.

(3) There would be a permanent appropriation on a percentage basis, thus placing the bill under the jurisdiction of the House Ways and Means Committee and bypassing the annual appropriation procedures.

(4) A greater proportion (roughly half) of the shared funds would go to local governments under the revised plan.

(5) Two factors would be used to determine how much money should go to each state: the size of the population and the degree to which it has already utilized its own tax resources.

(6) Two options were available for determining the distribution of funds within a state: use of a formula to be prescribed by the Federal government or use of a formula that the states would negotiate with their local governments. A bonus of 10 percent would be paid to those states developing their own distribution formula acceptable to the Federal government. All funds going to local governments would be channeled through the state government.

(7) Governmental units of all sizes would be eligible for aid.

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[1]"Text of President's Message on Revenue Sharing," Congressional Quarterly, Weekly Report, February 12, 1971, Vol. XXIX No. 7, p. 393.

(8) General revenue sharing funds would be distributed with no program or project restrictions, at either the state or local level.

Senator Muskie's Proposal

Senator Muskie's bill (S 1770), introduced for the second time in early 1971, proposed sharing $6 billion in Federal revenues the first year, $1 billion more than the Nixon plan.[1] Other major provisions differing from the Administration bill were:[2]

(1) Apportionment of funds among local governments on the basis of need, as well as population and tax effort, which were common to both bills.

(2) A bonus, equal to 10 percent of a state's income tax collections, to encourage the adoption of state income taxes.

(3) Provisions for stronger safeguards against discrimination in the use of revenue sharing funds. A mechanism for individual or class action suits was included.

(4) Authorization of five-year appropriations, a means of financing the program which would keep jurisdiction over it in the Government Operations and Appropriations Committees. The House Ways and Means Committee and the Senate Finance Committee had jurisdiction over the Nixon plan because it involved automatic sharing of a proportion of Federal revenues.

The most significant differences between the Nixon plan and the Muskie plan were, therefore, that Muskie's contained the incentive for state income taxes, provided for specific dollar appropriations over a limited period of time, and interjected need as one of the criteria for distribution of funds.

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[1] "Revenue Sharing," Congressional Quarterly, Weekly Report, June 4, 1971, Vol. XXIX No. 23.

[2] Ibid.

Senator Humphrey's Proposal

Senator Hunphrey's bill (S 241) closely paralled that of Senator Muskie, providing $3 billion in the first year and $5 billion each year thereafter, with appropriations to be made annually.[1] His bill also contained the state income tax incentive, but in addition contained an incentive for the modernization of state and local governments as a condition of participation by the state governments. This was an explicit recognition of the inefficient structure of many local governments. Since state government possess the power to regulate city and county boundaries and the incorporation of these units of government, Senator Humphrey sought to force the state government to correct organizational inefficiencies of the local governments within the states.[2]

A tabular comparison of the revised Nixon plan, the Muskie and Humphrey proposals, and the Mills plan, which came several months later, is contained in Appendix I.

Support for Revenue Sharing Legislation

As noted previously, support for some type of revenue sharing had come from prominent politicians of both parties at various times over the last decade. Both the Republican and

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[1] U.S. Congress. Senate. Committee on Government Operations. Intergovernmental Revenue Act of 1971 and Related Legislation. Hearings before the Subcommittee on Intergovernmental Relations of the Committee on Government Operations, Senate, on S. 1770 and S. 241, 92nd Cong., 1st sess., 1971, p. 35.

[2] Ibid.

Democratic presidential nominees endorsed the concept in the 1968 election, and in the 1969-1971 period, the President and Senators Muskie and Humphrey had introduced bills to institute such a program.

Interest in the program was sustained by the intense lobbying efforts of the U.S. Conference of Mayors and the National League of Cities.[1] By early 1971 many members of Congress had become convinced that they should join the revenue sharing bandwagon. They expected to gain politically from the distribution of Federal funds in their states and districts. Realizing that the regular and continuous dispensing of funds achieves the maximum political effect, most members of Congress became mesmerized by this feature of revenue sharing.

Opposition to Revenue Sharing

While many Senators and Congressmen had joined the growing movement in favor of revenue sharing during 1970 and the first half of 1971, one crucial holdout remained: Chairman Wilbur D. Mills of the House Ways and Means Committee. Mr. Mills was more than a holdout--he was the foremost critic of revenue sharing. In an address to the Louisiana legislature on June 1, 1971, Mr. Mills said he was planning a quiet funeral for the Nixon revenue-sharing bill as soon as his committee completed hearings on it.[2]

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[1] Revenue Sharing Advisory Service, Inc., Revenue Sharing Bulletin, November 1972, Vol. 1, No. 1, Washington, D.C., p. 8.

[2] "Revenue Sharing," Congressional Quarterly, Weekly Report, June 4, 1971, Vol. XXIX No. 23, p. 1214.

Chairman Mills was joined in his opposition to revenue sharing by the ranking Republican on the Ways and Means Committee, Mr. John W. Byrnes. At a news conference on June 2, Mr. Mills predicted, as he had several times previously, that the committee would not approve the bill. Mr. Mills was opposed not only to the Administration's bill, but to any form of revenue sharing. "I am not convinced," he said, "that the states are in worse condition than we are here in Washington."[1]

Chairman Mills specific objections to the Administration's general revenue sharing program were:[2]

(1) The Administration's general revenue sharing plan would distribute funds to all local governments on the basis of their tax collection and not on the basis of need.

(2) Without "strings attached," revenue sharing would completely divorce the responsibility for raising revenue from the spending of revenue.

(3) Revenue sharing would add another "uncontrollable" expenditure to the Federal Budget.

(4) Revenue sharing would do nothing to encourage state and local governments, which were in financial difficulty, to help themselves.

In August, 1971, representatives of the National League of Cities and the U.S. Conference of Mayors met with Chairman Mills to discuss his opposition to the Administration's bill and possible alternatives. Mr. Mills apparently became convinced of the political volatility surrounding the drive for revenue sharing legislation, because he shortly reversed his previous

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[1] Ibid.

[2] Ibid.

stand and committed himself to work for some type of program.[1]

Chairman Mills' subsequent actions brings to mind a bit of philosophy once expounded by the late Senator Everett Dirksen. Senator Dirksen once observed that if it looks like you're about to get run out of town on a rail, then get out in front and make it look like you're leading a parade. That is precisely what Mr. Mills did. Once he had changed his mind, he was determined that the final product would be his bill.

Mr. Mills had actually begun to reconsider his stand against revenue sharing before the August meeting with the National League of Cities and the U.S. Conference of Mayors. On June 9, only one week after his avowed plans to bury the bill, Chairman Mills held a closed meeting of Democratic Congressional and party leaders in which he discussed an alternative plan to the Administration's proposal. He described this as preliminary thinking which was subject to negotiation with committee members.[2]

Following this meeting and the negotiations in August with the U.S. Conference of Mayors and the National League of Cities, Mr. Mills instructed his staff to work with these two organizations, as well as with representatives of the governors, legislators and the counties to develop a compromise bill.[3]

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[1] Revenue Sharing Advisory Service, Inc., Revenue Sharing Bulletin, November 1972, Vol. 1, No. 1, Washington, D.C., p. 8.

[2] "Revenue Sharing: Mills' Plan for Aid to Cities," Congressional Quarterly, Weekly Report, June 11, 1971, Vol. XXIX, No. 24, p. 1308.

[3] "General Revenue Sharing: Giveaway or Godsend?" Congressional Quarterly, Weekly Report, May 6, 1972, Vol. XXX, No. 19, p. 1000.

Upon completion of the work conducted jointly by Mr. Mills' staff and the various representatives of lower echelon governments, Congressman Mills introduced the Intergovernmental Fiscal Coordination Act of 1971 (HR 11950) on November 30, 1971.[1] The final bill that emerged from the Committee bore a different title, inasmuch as it was rewritten in committee to some extent, but the provisions of the bill were nearly identical in concept to the original Mills bill (HR 11950).

Congressman Wilbur D. Mills' Proposal

After deciding that he would support a revenue sharing bill, Chairman Mills announced that he favored a plan that would give more benefits to urban areas and less to state governments. Mr. Mills concluded that localities were facing the most severe financial conditions and that there were very few taxation measures available to them to solve their own problems. On the other hand, he concluded that many state governments were not making effective use of their revenue sources, either by not employing certain taxes, such as individual and corporate income taxes and general sales taxes, or by keeping rates too low. His bill therefore would distribute the funds on the basis of need to state and local governments. In keeping with this goal, the bill provided that two-thirds of all revenue sharing funds would go to local governments and one-third to state governments.[2] Under President

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[1] Ibid.

[2] Ibid.

Nixon's revised bill, about 48 percent would have gone to local governments, and under his original proposal, even less was slated for local governments.[1]

The bill contained a complex distribution system that encouraged both total tax effort and state income taxes. It specifically encouraged the adoption of state income taxes in much the same manner as the Muskie and Humphrey plans had suggested.[2]

Rather than be an "open ended" program as was the Nixon proposal, Mr. Mills program would be of limited duration, a five year period of time. Additionally, rather than embracing an "uncontrollable" appropriation in the Federal budget of a fixed percentage of Federal revenues, as the Nixon plan had proposed, the Mills plan allocated a fixed dollar amount for each of the five years, with $3.5 billion to local governments and $1.8 billion to state governments during the first year. This amount would be increased by $150 million for the second year and $300 million for each succeeding year for the rest of the five-year period.[3]

This provision concerning a fixed amount of money each year is particularly interesting in that the only reason the Ways and Means Committee had jurisdiction over the legislation was that the Nixon bill had provided for a percentage of revenues rather than a fixed dollar amount. With the Mills proposal now rejecting the percentage concept and providing for the fixed sums,

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[1] Ibid. [2] Ibid. [3] Ibid., p. 1001.

the revenue sharing legislation should have been treated as any other appropriations measure. This would mean that the Ways and Means Committee would no longer have jurisdiction over the bill and that the House Appropriations Committee would assume that authority. Mr. Mills was determined, however, that any revenue sharing legislation reported to the House floor would not only bear his stamp, but would also be closed to amendment from the floor. As will be discussed in greater detail later, this precipitated a struggle between the Ways and Means Committee, Appropriations Committee, and House Rules Committee.

The Mills bill also set both a floor and a ceiling for amounts to be received by local governments. Any locality whose allocation amounted to less than $200 would receive nothing at all, a limitation imposed to discourage the incorporation of small hamlets for the purpose of sharing in the Federal bounty. It placed a ceiling on the total allocation to any locality of 50 percent of the unit's taxes and transferred funds.[1]

The Mills bill also attached more "strings" to the funds shared with local governments than did the Administration's proposal.[2] Many members of Congress, and particularly Mr. Mills, regard supervision of the use of Federal funds as their perogative and responsibility. They take the position that it is their duty to establish the conditions under which _any_ grant of Federal money is to be spent. Therefore, the Ways and Means Committee was not in agreement with the granting of carte blanche to state

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[1] _Ibid._, p. 1002. [2] _Ibid._, p. 1002.

and local governments for the expenditure of revenue sharing funds.

Expenditures under the Mills program would be limited to financing local items designated as national high priority needs by the Federal government , i.e., the Ways and Means Committee. These priority items included public safety, environmental protection, public transportation, youth recreation programs, health administration, and related capital programs.[1]

The major differences in philosophy between the President's revised plan and Mr. Mills' proposal have been explored, but the details of the latter will not be discussed here. Chapter V will discuss the details of the final bill adopted by the Congress, and as previously indicated, except for minor adjustments the final legislation was identical to the bill introduced by Mr. Mills. Final action by the Ways and Means Committee was completed on April 17, 1972, when the committee voted 18-7 to report the State and Local Fiscal Assistance Act of 1972 (HR 14370).[2] The designation of the bill had been changed during committee processing to reflect a broader base of participation by committee members, even though no important changes had been made to the bill drafted by Mills himself (HR 11950).

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[1] Ibid., p. 1002.

[2] "General Revenue Sharing: Giveaway or Godsend?" Congressional Quarterly, Weekly Report, May 6, 1972, Vol. XXX, No. 19, p. 1000.

Clash Between the Ways and Means and House Appropriations Committees

Having overseen the adoption of his own proposal by the House Ways and Means Committee, Chairman Mills was determined that this version of revenue sharing legislation would prevail. There were, however, nearly as many revenue sharing proposals floating around Capitol Hill as there were constituencies represented. Each Senator and Congressman was in favor of a distribution formula that would favor his own particular state or district. For example, Senator Baker of Tennessee, who had introduced the revised Nixon plan in the Senate as S 680, and Senator Gurney of Florida, both represent states having a constitutional prohibition against a state income tax and were opposed to any distribution formula that would penalize their states for not having this type of tax.[1] The Congressmen from these states would naturally attempt to amend the bill from the floor to lessen the incentive for state income taxes. There were many other special interests that members of Congress could be expected to protect by amendment from the floor.

Chairman Mills, therefore, deemed it essential that the committee bill be reported to the House floor as a closed bill, meaning that only amendments from the Ways and Means Committee would be in order when the bill came before the House. This

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[1] U.S. Congress. Senate. Committee on Government Operations. Intergovernmental Revenue Act of 1971 and Related Legislation. Hearings before the Subcommittee on Intergovernmental Relations of the Committee on Government Operations, Senate, on S. 1770 and S. 241, 92nd Cong., 1st sess., 1971, pp. 46, 103.

would also waive points of order against the bill. Bills from the Ways and Means Committee, usually tax bills, are often granted closed rules because of their complexity.[1]

Appropriations Committee Chairman George Mahon vigorously objected to the reporting of a closed bill in this instance.[2] The Ways and Means Committee had originally exercised jurisdiction over the revenue sharing program because the bill introduced on behalf of the Nixon Administration featured the distribution of a percentage of Federal revenues. The program as revised by Mills, however, deleted that feature and instead allowed for the appropriation of a fixed sum of money in each of five years. Here, then, was a bill that had evolved into nothing less than a pure appropriations measure that not only bypassed Mahon's committee, but would be reported before the House as a closed bill that Mahon could not alter.[3]

Mahon was supported by Chairman William M. Colmer of the Rules Committee which has the authority to rule on such matters.[4] A third faction was led by Congressman Henry S. Reuss who had co-sponsored the Humphrey revenue sharing plan the previous year. Reuss sought to use the revenue sharing bill as a vehicle for tax reform, and to do this it was necessary for the bill to be open to amendment on the House floor.[5] Mills, however, with the support of Speaker Carl Albert, won the closed rule by an 8-7 vote

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[1]"Revenue-Sharing Bill Delayed," Congressional Quarterly, Weekly Report, May 27, 1972, Vol. XXX, No. 22, p. 1224.

[2]Ibid. [3]Ibid. [4]Ibid. [5]Ibid.

of the Rules Committee on May 23, 1972.[1]

Chairman Mahon was livid. On June 7, he voiced his objections as follows:[2]

> Next week there is also scheduled to be before the House a $30 billion appropriation bill out of the Ways and Means Committee.
>
> Mr. Speaker, this Ways and Means Committee bill does not raise one penny of revenue. It is an authorization bill and it is an appropriation bill for five years. It bypasses the established authorization process involving a number of major legislative committees, and it bypasses the established appropriations process which we have known for the last 52 years.
>
> Not in the history of Congress that I can find has an appropriation bill come to the floor under a closed rule which is now proposed for this Ways and Means Committee bill.
>
> I say it is indefensible that the appropriation bill of $30 billion should come before the House next week under a closed rule. Members should have the right to make points of order and offer amendments. I propose to do what I can to open up the rule so the House can work its will on that appropriation bill, just as it does on other appropriation bills.

Mr. Mahon never had the opportunity to influence the bill, because the House supported the closed rule by a vote of 223-185 on June 21.[3] This action virtually assured passage of the bill. The closed rule limited action on the House floor to the alternatives of passing the bill, killing it, or returning it to the Ways and Means Committee. With governors, mayors, and other state

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[1] Ibid.

[2] "Revenue-Sharing Bill," Congressional Quarterly, Weekly Report, June 10, 1972, Vol. XXX, No. 24, p. 1372..

[3] "House Passes Revenue-Sharing Bill Without Amendment," Congressional Quarterly, Weekly Report, June 24, 1972, Vol. XXX, No. 26, p. 1565.

and local officials and their organizations lobbying vigorously for the bill with strong support from taxpayers, anything but passage of the bill was unthinkable. The bill commanded an impressive majority of 274-122 on a roll-call vote on June 22.[1] Debate had been limited to eight hours by the closed rule. The Mills bill now went to the Senate.

Senate Hearings on the House Approved Bill

The Senate Finance Committee started hearings on the revenue sharing bill on June 29.[2] The Administration took this opportunity to try to reverse some of the changes that the Ways and Means Committee had made to President Nixon's plan. Speaking for the Administration, Treasury Secretary George P. Shultz endorsed the bill, specifically acquiescing to the fixed dollar allocation over a period of five years, but asked for the following changes:[3]

(1) Removal of the state income tax incentive from the bill and restoration of Mr. Nixon's plan which rewards overall state and local tax effort, regardless of source.

(2) Removal of the House-imposed series of high-priority categories and restoration of the President's proposal requiring only that the funds be used for legitimate governmental purposes and in a nondiscriminatory fashion.

(3) Dilution of the urbanized population factor to distribute the funds among the states. This factor discriminated

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[1] Ibid.

[2] U.S. Congress. Senate. Committee on Finance, Revenue Sharing. Hearings before the Committee on Finance, Senate, on H.R. 14370, 92nd Cong., 2d sess., 1972, p. 1.

[3] Ibid., p. 75.

against states without urban populations, such as Alaska, Vermont, and Montana.

Senator Baker of Tennessee also testified against the income tax incentive, pointing out that Tennessee has a constitutional prohibition against such a tax. He introduced an amendment to reflect the Administration's stand on this particular point.[1]

The Senate Finance Committee was most receptive to the suggestions of Secretary Schultz and Senator Baker. Due to the nature of Senate constituencies, there were many Senators who opposed giving the urbanized states more money and wanted to eliminate the state income tax incentive.[2]

The Senate Finance Committee reported an amended version of HR 14370 to the Senate floor on August 9.[3] This bill reduced the amount of funds to be granted to urbanized states and increased funds for less populous states, but at the same time maintained funds for the major cities. This sounds somewhat contradictory, but is consistent if one distinguishes between urbanized areas, which includes suburbs, and the cities themselves.

In addition to deleting the urbanization factor from the allocation formula developed by the House, the Senate Finance Committee also deleted the state income tax incentive.[4] These

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[1] Ibid., pp. 105-110.

[2] Ibid., pp. 111-125.

[3] "Revenue Sharing," Congressional Quarterly, Weekly Report, August 12, 1972, Vo. XXX, No. 33, p. 2016.

[4] Ibid.

two changes, if enacted, would reduce the amount to be received by heavily urbanized states in which income taxes provide a major share of state revenues (such as New York and California) to about half the amount that would be received under the House bill.[1]

The Committee accepted the amount of money and the five year period of time established by the House bill, but dismantled the complicated formulas the House bill provided for the distribution of funds.[2] The House had established a "five-factor formula," which will be explained in detail in Chapter V, for distributing revenue sharing funds. The Finance Committee decided to distribute funds according to three factors: population, total tax effort, and inverse per capita income.[3] This reflected the decision to eliminate the urbanization factor and the income tax incentive and supported Mr. Mills' contention that allocation should also be based on need. In summary, the changes generally were to the advantage of the less-urbanized and less-wealthy states. Most members of the Senate Finance Committee, like Chairman Russell Long of Louisiana, represent states in this category.

Under the distribution formula proposed by the Committee, 33 states would receive more than under the House bill, and 17 states plus the District of Columbia would receive less. Of the

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[1]H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Finance, U.S. Senate, Report Together with Additional and Minority Views (to Accompany H.R. 14370), p. 13.

[2]Ibid.

[3]Ibid., pp. 12-13.

16 states represented on the Committee, 13 would receive more under this version.[1]

The Finance Committee decided to use the same formula for distribution of funds to local governments within the states.[2] In this manner major cities were provided for generously while the amount for suburbs was reduced.

The Committee also eliminated the restrictions on use of funds that the House bill had imposed.[3] This would have allowed funds to be used for education and welfare, activites prohibited by the House restrictions.

At the urging of Senator Lee Metcalf of Montana, the Committee also agreed to make Indian tribes eligible to share in the funds allocated to local governments.[4] This did not represent much of a change from a strictly monetary viewpoint, but it is indicative of the many social and political considerations of a bill of this nature.

Many other suggestions made to the Committee during the hearings were of course rejected. For example:[5]

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[1] "Revenue Sharing," Congressional Quarterly, Weekly Report, August 12, 1972, Vol. XXX, No. 33, p. 2016.

[2] H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Finance, U.S. Senate, Report Together with Additional and Minority Views (to Accompany H.R. 14370), pp. 14-15.

[3] Ibid., p. 16.

[4] Ibid., p. 23.

[5] "Senate Rejects Major Changes in Revenue-Sharing Bill," Congressional Quarterly, Weekly Report, September 9, 1972, Vol. XXX, No. 33, p. 2316.

(1) Mr. Roland M. Bixler, president of J.B.T. Instruments of New Haven, Connecticut, speaking for the National Association of Manufacturers, urged the incorporation of an amendment that would give businesses some type of relief from the differing state and local taxes.

(2) Mr. Paul Parks, administrator of the model cities program in Boston, speaking for Americans for Democratic Action, supported revenue sharing for local governments but wanted to eliminate distribution of funds to the state governments.

(3) Senator James L. Buckley of New York proposed that revenue sharing per se not be adopted, suggesting an alternative plan under which the Federal government would shift part of its personal income tax base to the states and share its tax-collecting facilities to help the states collect their own income taxes.

Many interest groups opposed the bill entirely. In a moment of rare agreement both business and labor interests testified against adoption of any kind of revenue sharing legislation. Mr. Bixler, who had urged the adoption of the tax relief amendment for businesses, actually opposed the bill completely, but realizing it would probably pass, was attempting to make it as palatable as possible. Mr. Eugene F. Rinta, Executive Director of the Council of State Chambers of Commerce, opposed the bill on principle, and Mr. Andrew J. Biemiller, Director, Department of Legislation, AFL-CIO, opposed it on grounds of impracticability as well as on principle.[1]

Clash Between the Senate Finance Committee and the Senate Appropriations Committee

After approval of the revenue sharing bill by the Senate

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[1] H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Finance, U.S. Senate, Report Together with Additional and Minority Views (to Accompany H.R. 14370), pp. 387, 450, 407.

Finance Committee, a struggle took place between the Finance Committee and the Appropriations Committee, similar to that between Mills and Mahon in the House.[1] The Senate struggle was much less intense, however, and was resolved without the show-down over rules that had characterized the situation in the House.

On August 10, the day after the Finance Committee ordered the bill reported, the Appropriations Committee, under the new leadership of Senator John L. McClellan of Arkansas, voted to demand an opportunity to consider the bill before it went to the floor.[2] McClellan's demand was based on the same feature of the bill that Mahon had cited, i.e., that dollar amounts specified in the bill constituted an appropriations measure over which his committee should have jurisdiction.

To counter this move, Senator Long's committee on August 11 voted to rescind its previous action and not report the bill to the floor.[3] Senator Long was determined, as Congressman Mills had been, that the bill should not be subject to annual or periodic appropriations which would expose revenue sharing to pressures both from recipients and from conflicting claims of other Federal programs.

Noting that other trust-funded programs, such as Social Security, were financed under permanent appropriations and did

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[1] "Senate Rejects Major Changes in Revenue-Sharing Bill," Congressional Quarterly, Weekly Report, September 9, 1972, Vol. XXX, No. 37, p. 2316.

[2] Ibid. [3] Ibid.

not require annual appropriation action by the Congress, the Finance Committee circumvented Senator McClellan's committee by simply redrafting one provision of the bill. It removed the dollar appropriations and provided a "permanent" appropriation of 7 percent of personal income tax receipts of a special revenue-sharing trust fund for the five-year life of the program.[1] This action in essence reinstated the method of funding that had originally been proposed by the President, but placed it in direct opposition to the desires of Chairman Mills.

Confident that the amended bill had sufficient support to reject any effort by the Appropriations Committee to take control of it on the floor, the Finance Committee reported the bill to the Senate floor for the second time on August 16. Unlike the situation in the House in which the bill went to the floor under closed procedures, the Senate bill was open to amendment from the floor.[2]

Some minor amendments were adopted from the floor. One offered by Senator Vance Hartke of Indiana applied Federal labor standards to projects and government positions financed with revenue sharing funds.[3] Another amendment by Senator Long was adopted to dilute somewhat the Hartke amendment.[4] Long's amendment restricted the wage requirements of the Hartke amendment

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[1] Ibid.

[2] "Senate Revenue-Sharing Bill Favors Small, Rural States," Congressional Quarterly, Weekly Report, September 16, 1972, Vol. XXX, No. 38, p. 2352.

[3] Ibid. [4] Ibid.

to projects or positions for which more than 25 percent of the funding came from revenue sharing money.[1] Senator Hubert Humphrey, the perennial labor devotee, attempted to counter Long's 25 percent restriction with an amendment of his own that would have exempted the construction of sewage and refuse disposal systems and transportation systems from the 25 percent limit. This attempt was unsuccessful, being defeated by a vote of 46-39.[2]

Another amendment by Humphrey was adopted, a noncontroversial proposal directing the Joint Committee on Internal Revenue Taxation to prepare a report by June 30, 1973, on real estate and property tax administration.[3]

Several amendments were also rejected, the most important one being an attempt by Senator McClellan, once again, to gain control of the appropriations aspect of the bill. By a 34-49 vote the Senate rejected McClellan's bid to require the Appropriations Committee's approval of revenue sharing funds for the last three years (fiscal 1974-1976) covered under the bill.[4] An amendment by Senator Ribicoff altering the committee formula for allocation of funds to the states was defeated 24-61.[5] Senator Ribicoff wanted to reinstate the formula that would favor urbanized populations, the same formula passed by the House but changed by the Senate Finance Committee. The rural states clearly

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[1] *Ibid.* [2] *Ibid.* [3] *Ibid.* [4] *Ibid.* [5] *Ibid.*

prevailed over the urban states in the Senate. Predictably, the 24 Senators voting for the Ribicoff amendment were from states whose shares would have been enlarged by his formula.

Two amendments offered by Senator Hartke were also defeated. One would have prohibited the use of revenue sharing funds to induce a business or industry to move a factory or other facility from one area to another. The second would have applied the labor requirements of the 1964 Urban Mass Transportation Act to any urban mass transportation systems acquired by governmental units with Federal revenue sharing funds.[1] Southern Senators were instrumental in the defeat of both of these amendments.

On September 12, 1972, the Senate passed the revenue sharing bill by a 64-20 vote.[2] The final bill was substantially the same as reported by the Finance Committee, a bill favoring the small, rural states, and one imposing minimal controls on the usage of funds.

Final Compromises in the Conference Committee

The major provision of the bill to be settled by the House and Senate conferees was the matter of distribution formulas. The House version of the bill, based on five factors, had provided larger amounts to the more populous, urban states and had contained an incentive for states to employee an income tax. The Senate version, based on three factors, favored the less populous, rural states and contained no income tax incentive.

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[1] Ibid. [2] Ibid.

Since neither side was willing to abandon completely the formula developed by its legislative branch, an unusual compromise was adopted that allowed each state the larger of the two amounts available under the different formulas approved by the House and Senate. With each state given the higher of two possible shares, total funding would obviously exceed the amount appropriated for each of the five years. Therefore, to offset this increase, the conference agreement provided for a proportional reduction of each state'a allocation to keep the total within the established limits for each year.[1]

While allowing a choice between two methods of determining how much Federal revenue would go to all governments within a state, the conferees adopted the Senate's version for determining how the state total would be distributed among the state government and the various local governments within the state.[2]

Another matter to be settled was the differences over usage of funds by state and local governments, with the House version favoring fairly strict limitations on usage by both state and local governments, and the Senate version favoring practically no restrictions on either. The conference committee agreed to a provision that would place restrictions on local governments but not on state governments.[3]

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[1]H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee of Conference, U.S. Senate - House of Representatives, Conference Report (to Accompany H.R. 14370), Sec. 106.

[2]*Ibid.*, Sec. 107.

[3]*Ibid.*, Sec. 103.

Reflecting the amendment that had been offered by Senator Lee Metcalf during debate of the bill on the Senate floor, the conference agreement included a provision allocating part of a county area's allotment to the governing bodies of local Indian tribes or Alaskan native villages that performed substantial governmental functions. The Senate floor amendment had set aside 0.25 percent of total revenue sharing funds for Indian tribes and Alaskan natives, but the conference agreement provided an allocation on the basis of population as a percentage of the county population.[1]

The conference agreement also approved specific dollar appropriations rather than the percentages adopted by the Senate before reporting the bill to the Senate floor the second time.[2] This had been a ploy to keep control of the bill within the Senate Finance Committee and out of the hands of Senator McClellan's committee. Once the bill had passed the Senate and gone to the conference committee, there was no need to retain the percentage feature in the legislation.

The House and Senate conferees filed a conference report on September 25, signifying final agreement on the revenue sharing bill. Congress accepted the conference version on October 13 by a vote of 59-19 in the Senate and 265-110 in the House.[3]

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[1] *Ibid.*, Sec. 108.

[2] *Ibid.*, Sec. 105.

[3] "Congress Clears Nixon's Revenue-Sharing Plan," *Congressional Quarterly, Weekly Report*, October 7, 1972, Vol. XXX, No. 41, p. 2636.

To dramatize what he called the "New American Revolution," President Nixon signed the State and Local Fiscal Assistance Act of 1972 into law at Independence Hall in Philadelphia on October 20, 1972, stating, "It is appropriate that we launch this New American Revolution in the same place where the first American Revolution was launched by our founding fathers 196 years ago."[1]

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[1] The Washington Star-News, October 20, 1972, p. 5, Col. 1-3.

CHAPTER V

PROVISIONS OF THE STATE AND LOCAL FISCAL ASSISTANCE ACT OF 1972

This chapter focuses on the major aspects of the Revenue Sharing Act, and though an occasional analysis in interjected in this part of the paper, critical comments are confined primarily to Chapter VII.

In general terms, the act distributes money on the basis of census data and other objective statistics and provides for a distribution of funds over a five year period of time. The money will be automatically available for each of these five years, so state and local governments can count on the revenue in their own fiscal planning. One-third of the revenue going to a state will be received by the state government and two-thirds by the local governments within the state.[1]

Appropriations

The Revenue Sharing Act creates a trust fund known as the "State and Local Government Fiscal Assistance Trust Fund" and provides for the appropriation to this Trust Fund from the general fund of the U.S. Treasury a total of $30.2 billion over

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[1] State and Local Fiscal Assistance Act of 1972, Secs. 107, 108, 86 Stat. 919 (1972).

a period of five years. These funds are automatically released to the Treasury for distribution, and will not be subject to the annual appropriation procedures.[1]

The appropriations, covering a period of time from January 1, 1972 through December 31, 1976, are as follows:[2]

January 1, 1972 through June 30, 1972	$2.7 billion
Fiscal year beginning July 1, 1972	5.6 billion
Fiscal year beginning July 1, 1973	6.0 billion
Fiscal year beginning July 1, 1974	6.2 billion
Fiscal year beginning July 1, 1975	6.4 billion
July 1, 1976, through December 31, 1976	3.3 billion

Assurances to the Secretary of the Treasury

In order to qualify for Revenue Sharing funds allocated for the period January through June, 1973, and thereafter, local governments must submit assurances to the Secretary of the Treasury that certain terms and conditions of the law will be met. The law requires that the assurances also be submitted to the Governor of each state for review and comment. Each unit of local government must establish to the satisfaction of the Secretary that it will:[3]

(1) Establish a trust fund in which all payments of funds, and interest earned thereon, will be deposited.

(2) Use these amounts during the period of time established by the Secretary.

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[1] Ibid., Sec. 105.

[2] State and Local Fiscal Assistance Act of 1972, Sec. 105, 86 Stat. 919 (1972).

[3] Ibid., Secs. 121, 122, 123.

(3) Expend these funds only for uses permitted by the Act.

(4) Make expenditures from these funds only in accordance with laws and procedures applicable to its own funds.

(5) Use fiscal, accounting, and audit procedures conforming to guidelines established by the Secretary.

(6) Provide the Secretary and the Comptroller General of the U.S. with access to books, documents, papers, or records for purposes of reviewing compliance.

(7) Make all annual or interim reports required by the Secretary.

(8) Pay wages to employees out of general revenue sharing funds at the same rates it pays other employees in similar occupations.

(9) Assure that laborers and mechanics employed by contractors on a project funded in part with revenue sharing funds are paid according to the provisions of the Davis-Bacon Act.

The requirements listed above were established to enable the Secretary of the Treasury to make periodic compliance studies and to assist Congress in determining whether the revenue sharing program should be continued, revised, or terminated at the end of the initial five-year period. The Secretary of the Treasury will report to the Congress not later than March 1 of each year on the operation and status of revenue sharing allocations during the previous year.[1]

Reports to the Secretary of the Treasury

Each unit of local government which expects to receive funds after January 1, 1973, must submit a report to the Secretary

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[1]*Ibid.*, Sec. 105.

setting forth the amounts and purposes for which it plans to use the funds. This report is to be submitted before the beginning of each entitlement period and must be submitted in the form and detail prescribed by the Secretary. Then after the close of each entitlement period, a report on how the funds were actually used must be submitted. Additionally, the reports must be made available to the public by publishment in a newspaper which has general circulation within the area.[1]

Restrictions on the Use of Revenue Sharing Funds

Only minimal restrictions have been applied to the use of revenue sharing funds. Two general restrictions apply to both state and local governments: Funds cannot be used for matching funds for Federal grant-in-aid programs, nor may they be used for projects or programs which discriminate on the basis of race, color, sex or national origin.[2] These restrictions are the only ones imposed on the state governments. Local governments have the additional prohibition that revenue sharing funds may not be used for educational purposes other than libraries. Additionally, local governments must use their funds only for "priority expenditures," which under the provisions of the act are defined as:[3]

1. Ordinary and necessary maintenance and operating expenses for:

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[1] *Ibid.*, Sec. 121.

[2] *Ibid.*, Secs. 104, 122.

[3] *Ibid.*, Sec. 103.

a) public safety (including law enforcement, fire protection, and building code enforcement)

b) environmental protection (including sewage disposal, sanitation, and pollution abatement)

c) public transportation (including transit systems and streets and roads)

d) health

e) recreation

f) libraries

g) social services for the poor or aged

h) financial administration

2. Ordinary and necessary capital expenditures authorized by law.

Although local governments are required to use their money for these categories of expenditures specified by the act, the categories are of such a general nature that a great deal of latitude exists in the expenditure of revenue sharing funds.

Maintenance of Support by State Governments

To ensure that state governments do not use revenue sharing as an excuse to curtail support to local governments, the bill requires that each state must provide as much support to the local governments as it did during Fiscal Year 1972. Beginning July 1, 1973, any state government which reduces its aid below the level of aid provided in Fiscal Year 1972 will have its revenue sharing allocation reduced accordingly.[1] This maintenance of support provision may be waived only if the state

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[1] Ibid., Sec. 107.

takes over certain functions which were previously the responsibility of local governments, or if it gives or transfers to local governments new taxing authorities.

Federal ("Piggyback") Collection of State Income Taxes

Provision is made in the Revenue Sharing Act for Federal collection of state income taxes at the request of state governments. If a state exercises this option, the Federal Government is to handle the administration of the state income tax. Under this provision, the Federal Government would collect the states' share in the withholding of income taxes from wages and salaries. Employers withholding state income taxes would pay them to the U.S. Treasury instead of to state treasuries, with the withheld funds being paid promptly to the states by the Federal Government.[1]

To take advantage of Federal collection of state income taxes, the state generally is to conform its income tax to the Federal tax. The state may either express its tax as a percentage of Federal income tax or apply the state income tax rates to the same base as Federal taxable income. In both cases, however, adjustments are to be made for state and municipal bond interest income, state income tax payments deducted for Federal income tax purposes, and Federal bond interest income.[2]

This provision is to go into effect on January 1, 1974, if at least five states accounting for at least five percent of

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[1] *Ibid.*, Sec. 202. [2] *Ibid.*

the taxpayers in the U.S. have requested Federal collection of their state income taxes.[1]

Several purposes of this provision are noted. One purpose is to achieve a degree of standardization of state and Federal income tax laws for those states opting for this collection service. Another is simply to provide a service to the states through the efficient collection mechanism of the Internal Revenue Service. A major purpose is to encourage the use and expansion of the state income tax as part of the stimulation of state and local tax efforts discussed in Chapter II.

Distribution of Revenue Sharing Funds

Due to conflicting interests in the House and Senate when the Revenue Sharing Bill was under consideration, two separate formulas were developed for determining an allocation for a state. The House formula favored the larger, industrialized states, and the Senate formula, predictably, benefited the smaller, more rural states. Rather than accept a compromise formula, Congress simply adopted both formulas, essentially allowing each state to take either the House grant or the Senate grant, whichever would be the more generous. Then on the related question of allocations within the states, the conferees chose the Senate formula which focuses funds on the cities and poor rural areas.[2]

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[1] Ibid., Sec. 204

[2] "Revenue Sharing: House-Senate Agreements Filed," Congressional Quarterly, Weekly Report, October 7, 1972, Vol. XXX No. 41, p. 2530.

The two formulas will be discussed in some detail to show how the specific allocations are determined. Then the hierarchical steps involved in the distribution will be illustrated by means of a chart.

The Senate formula, known as the "three-factor formula," distributes revenue by using a "population factor," a "general tax effort factor," and a "relative income" factor.

The "three-factor formula" for computing revenue sharing is as follows:[1]

Each state's share =

$$\frac{(\$5.3 \text{ billion}) \times (\text{population}) \times (\text{GTEF}) \times (\text{RIF}) \text{ of a state}}{\text{Sum of products of } (\text{population}) \times (\text{GTEF}) \times (\text{RIF}) \text{ of all states}}$$

where

$5.3 billion is the total amount available in 1972; this will vary somewhat in subsequent years

GTEF = General Tax Effort Factor =

$$\frac{\text{Net Taxes Collected (state and local)}}{\text{Aggregate Personal Income}}$$

RIF = Relative Income Factor =

$$\frac{\text{Per Capita Income of U.S.}}{\text{Per Capita Income of that state}}$$

Two important observations are made at this point. The first is that an increase in the GTEF would increase the share being received by a state, and that given a particular Aggregate

[1] *State and Local Fiscal Assistance Act of 1972*, Sec. 106, 86 Stat. 919 (1972).

Personal Income for that state, the only way to increase the GTEF is to INCREASE the level of state and local taxes. This is not to infer that a state would necessarily raise taxes in order to increase its proceeds from revenue sharing, but it does suggest that a state would be reluctant to cut its taxes and lose revenues through both the tax cut and the ensuing decrease in revenue sharing funds.

The second observation is that a high RIF is also favorable for a state and that the lower the per capita income of a state, the higher will be the RIF. Additionally, the lower the income of a state, the higher the GTEF, and consequently the higher the state's share. In summary, the "three-factor formula" favors those states with high population, high local taxes, and low income.

The far more complicated "five-factor formula" developed by the House divides the total amount of revenue to be shared into five parts, each determined on the basis of a different factor as follows:[1]

1. Population
2. Urbanized Population
3. Population Weighted Inversely for Per Capita Income
4. Income Tax Collections
5. General Tax Effort

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[1] *Ibid.*, Secs. 106, 107, 108, 109.

Each part is determined as follows (Note: the figures of \$3.5 billion and \$1.8 billion represent two-thirds and one-third, respectively, of the total amount available for 1972, and will vary somewhat in subsequent years):[1]

First Part: Each State's Share =

$$1/3 \text{ X } (\$3.5 \text{ billion}) \text{ X } \frac{\text{Population of State}}{\text{Population of All States}}$$

Second Part: Each State's Share =

$$1/3 \text{ X } (\$3.5 \text{ billion}) \text{ X } \frac{\text{Urban Population of State}}{\text{Urban Population of All States}}$$

Third Part: Each State's Share =

$$\frac{1/3 \text{ X } (\$3.5 \text{ billion}) \text{ X } \dfrac{\text{Population of State}}{\text{Population of All States}} \text{ X } \dfrac{\text{Natl. Per Capita Inc.}}{\text{State Per Capita Inc}}}{\text{Sum of Products of (State Population) X (National Per Capita Income)} \Big/ \text{(State Per Capita Income of All States)}}$$

Fourth Part: Each State's Share =

$$1/2 \text{ X } (\$1.8 \text{ billion}) \text{ X } \frac{\text{State Income Tax}}{\text{All Income Tax}}$$

Fifth Part: Each State's Share =

$$1/2 \text{ X } (\$1.8 \text{ billion}) \text{ X } \frac{\text{General Tax Effort Factor of State}}{\text{General Tax Effort Factor of All States}}$$

where

$$\text{General Tax Effort Factor} = \frac{\text{Net Taxes Collected}}{\text{Aggregate Personal Income}}$$

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[1] Ibid.

The following observations concerning the "five-factor formula" are made, considering each of the above parts separately:

(a) First Part - the higher the population of the state the greater will be its share.

(b) Second Part - the higher the urban population of the state the greater will be its share.

(c) Third Part - the lower the state per capita income the greater will be its share; additionally, greater population will increase this portion as well.

(d) Fourth Part - the greater the state income tax the greater will be its share.

(e) Fifth Part - the greater the general tax effort of the state the greater will be its share.

In summary, the "five-factor formula" favors those states with high urban populations, high local taxes, states with income taxes, and states with low income. The First, Second, and Third Parts each account for approximately 22 percent of the total amount a state receives, the Fourth and Fifth Parts accounting for 17 percent each. Perhaps the most important point is that the effect of high state taxes is given even more importance under this plan than under the "three-factor formula."

The two formulas discussed so far are used to determine the amount of money going to the state as a whole, not to the state government itself. Once this amount has been determined, one-third of it goes to the state government and two-thirds to the lower-echelon governments within the states, i.e., county city, township or other local units of government. Provision

is also made for Indians to receive allocations of revenue sharing funds.[1]

The allocation of funds to the local units of government is determined by using a variation of the "three-factor formula." The amount going to a county area is determined as follows:[2]

$$\text{County Area's Share} = 2/3\ (\text{State Share}) \times \frac{\text{County Population} \times (\text{GTEF}) \times (\text{RIF})}{\text{Sum of Products of (Population)} \times (\text{GTEF}) \times (\text{RIF}) \text{ for All Counties}}$$

Interestingly enough, the share for Indians in the county has first priority after the amount for the entire county area has been determined. This is calculated as follows:[3]

$$\text{Share for Indians in County} = \text{Total County Area Share} \times \frac{\text{Indian Population}}{\text{County Population}}$$

After the Indians' share has been deducted from the total county area share, the share for the county government itself is computed as follows:[4]

$$\text{County Government's Share} = \text{Remaining County Area Total} \times \frac{\text{Adjusted Taxes of County Government}}{\text{Adjusted Taxes of All Local Government Units in County, Including County Government}}$$

It can be seen from the above formula that the County Government's Share is based upon a proportional share of the county area

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[1] *Ibid.*, Sec. 108. [2] *Ibid.* [3] *Ibid.* [4] *Ibid.*, Sec. 108.

adjusted taxes. The shares for the townships and municipalities within the county are computed in exactly the same way, i.e., as a proportional share of the county area adjusted taxes.

An examination of the formulas for computing the County Area's Share and the County Government's Share reveals the same emphasis on tax collection at the local level that was discussed earlier in regard to the state allocations. That is, the higher a county's taxes the higher will be its share. It is also apparent that a county with a large Indian population could have much of its money allocated to the Indians rather than to the county government.

Chart I on the following page depicts diagrammatically the intrastate distribution of revenue sharing funds among the counties, townships, and municipalities of a state.

Change of Allocation Formulas

The Revenue Sharing Act includes a provision permitting states to modify the allocation formula to be used in distributing funds to the local units of government. This allows the states to shift the weight of general tax effort factors and relative income factors in the allocation of funds. A state may exercise this option just once during the five-year term of the program. Such action requires the enactment of a public law by the state. The state must also notify the Secretary of the Treasury not later than 30 days before the beginning of the first entitlement

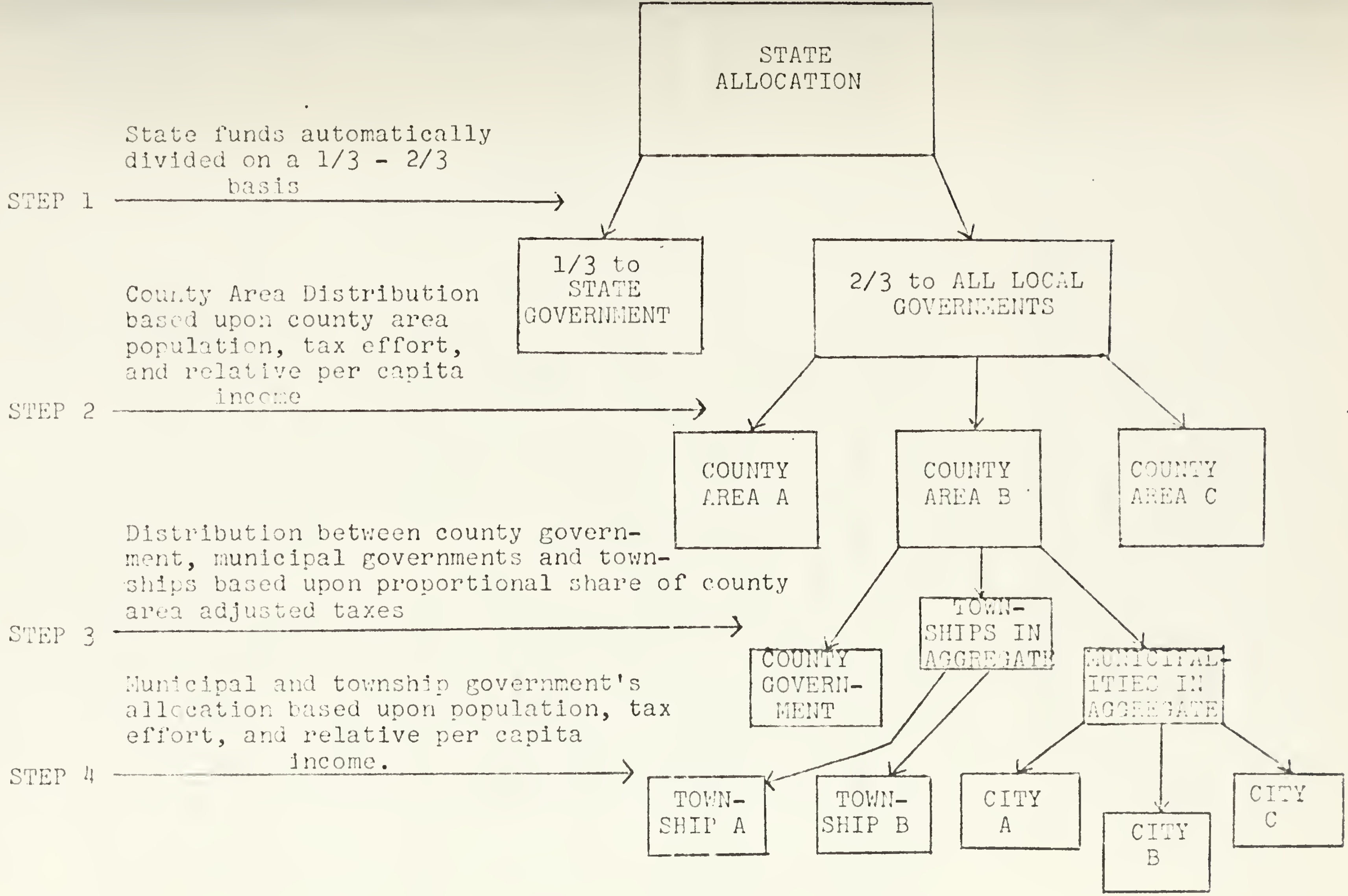

CHART I

INTRASTATE DISTRIBUTION OF REVENUE SHARING FUNDS

period to which the new law applies. The Secretary then will certify that the state law complies with all requirements of the local option formula, and that the law will allocate to local governments all funds to which they are entitled under the Act for each pay period through December 31, 1976. Any such law must apply uniformly throughout the state.[1]

Auditing

Auditing will be conducted by a staff of about 25 accountants who will be used to back up normal state, city, county and town audits. Of the 39,000 different governments entitled to revenue sharing funds each year, about 300 will receive routine audits on a statistical sample basis. In addition, there will be special audits in cases of irregularities, racial discrimination cases, and wage problem cases.[2]

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[1] Ibid., Sec. 108.

[2] Ibid., Sec. 123.

CHAPTER VI

PURPOSES FOR WHICH REVENUE SHARING FUNDS WILL BE USED

General

Information from several sources was used in order to draw conclusions concerning the uses to which revenue sharing funds are being, and will be, directed. Personal interviews were conducted with officials of some 40 local governments in 8 different states to solicit their opinions concerning the revenue sharing program and ascertain the intended disposition of funds under the program. Other information was obtained from the Council of State Governments, the Senate Subcommittee on Intergovernmental Relations, and various magazine and newspaper articles.

One common theme emerged from the personal interviews: local governments are proceeding on the assumption that revenue sharing is only a temporary program and that it will not be extended after its present five-year life. Some of the officials interviewed expressed the personal belief that the program would become permanent, but at the same time were unwilling to base their budgetary projections on this belief. Therefore, the overwhelming majority of local governments seem to

be directing their money toward capital improvements or programs of a limited duration, i.e., activities that will not require continuous funding over an extended period of time.

In regional briefings conducted for the benefit of local officials, the Office of Revenue Sharing has urged that a conservative approach be taken in the use of revenue sharing funds, and has presented certain suggested guidelines for expenditures, guidelines that emphasize the possible limited life of the program.[1] These guidelines are not binding at all, inasmuch as governmental units are free to spend their money in a wide range of programs, so long as the specific limitations of the 1972 Act are observed. Since the Office of Revenue Sharing is an agency of the Treasury Department, its advice on spending may reflect a tacit decision already made by the Administration to eliminate the revenue sharing program after the initial period elapses.

A noticeable shift in the attitude of local officials was observed in the interviews conducted in late January and February, as opposed to those conducted in December and early January. In the earlier interviews an optimistic, grateful attitude seemed to prevail. Officials spoke of how the new funds would allow them to complete certain projects that had been planned for some time, but for which there had been insufficient funds available. Revenue sharing would permit

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[1]Sarah S. Keseker, City Clerk, Hartselle, Alabama, private interview held December 26, 1972.

the local governments to build their new fire departments, police stations, recreational facilities, etc., without the imposition of new taxes. Almost without exception, the officials interviewed looked upon revenue sharing as a godsend.

In contrast to this earlier euphoria, however, the officials interviewed most recently tend to view the program with suspicion. While they are happy to be receiving money from Washington, there is apprehension that some other Federally supported programs may be curtailed. The budgetary confrontation that has emerged between Congress and the White House in recent weeks has clearly had an effect on local governments and their plans for use of revenue sharing funds.

In the earlier interviews most officials could point to tentative plans for which revenue sharing funds would be used, but in the later interviews a wait-and-see approach has emerged. Since there is no requirement to spend the money in the immediate future, there is a feeling that no definite plans should be made until the extent of cuts in other areas, if any, is known. Some governments, therefore, have deposited their funds in interest-drawing accounts with the intent of waiting a year or so before making the final decision as to their use.

In general, there seems to be very little predisposition by local governments to reduce taxes, though this is being done in some cases. The two reasons most often extended for

this stand were that revenue sharing funds would permit only a very small reduction in the tax rate, so small that most people would not realize the difference, and that a tax reduction was politically dangerous in that a tax increase would be necessary in a few years if the revenue sharing program is terminated. It was felt that voters would tend to forget the tax reduction after a couple of years. Additionally, most officials believe that their constituencies favor using the funds for "extras," projects that could not otherwise have been funded.

Local officials interviewed in December and early January credited revenue sharing for stabilizing the local tax rate, asserting that without this money a tax increase would have been inevitable. Those interviewed in late January and February reserved judgment on this point. Some felt that if Federal programs are cut in other areas, a tax increase might still prove necessary.

In summary, the early elation by local officials over the prospect of revenue sharing funds has given way to an attitude of cautious optimism at best, and deep pessimism at worst, concerning the ultimate benefits of the program. In the final analysis, revenue sharing may be the vehicle for a net reduction of Federal funds to local governments.

Intended Uses of Revenue Sharing Funds by Localities

A compendium of the interviews conducted in this survey is included in Appendix II. Some officials interviewed

merely indicated that no decision had been made concerning how their funds would be used. Brief and uninformative interviews of this type were not written up for inclusion in Appendix II.

A more definitive concept of how revenue sharing funds are expected to be used can be formed by consideration of the following examples:[1]

> (1) Gainesville, Florida, (pop. 64,510), will use its $807,248 from the first two payments (half received on December 1, 1972, and half on January 1, 1973) for capital expenditures, primarily street improvements, sewage systems, and recreational facilities. None will be applied toward tax reduction.
>
> (2) Alachua County, Florida, (pop. 104,764), of which Gainesville is the county seat, will use one-third of its funds each year for tax reduction. The reduction will amount to about one mill. The county is undecided on how to spend the remaining two-thirds, but probably in the general category of capital expenditures.
>
> (3) Hartselle, Alabama, (pop. 7,355), plans to avoid spending on programs of a continuing nature. Funds from the first two checks will be spent for street improvements, a new road grader, and a new dump truck.
>
> (4) Decatur, Alabama, (pop. 38,044), will place its revenue sharing funds in a supplement to the regular budget. One-third of the funds are to be used to upgrade presently underfunded departments, and two-thirds for capital expenditures, specifically street improvements, new fire department equipment, and a drainage project. Decatur has a moderate tax rate and does not intend to use any funds for tax reduction.
>
> (5) Huntsville, Alabama, (pop. 137,802), has deposited its funds in an interest-bearing account and has made no definite plans for its use, except that it will not be used for tax reduction.

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[1]Refer to interviews in Appendix II.

(6) East Granby, Connecticut, (pop. 3532), will use its money for capital expenditures that had already been planned: a road construction truck, a police cruiser, and land fill scales and a scale house for the town dump. East Granby's first two payments amount to $41,886.

(7) Suffield, Connecticut, (pop. 8,634), plans to use its funds for a new garage, a drainage project, and partial payment of a new bridge. According to the mayor, a tax increase would definitely have been necessary without these funds.

(8) Windsor Locks, Connecticut, (pop. 15,080), will use part of its funds for bond reduction and part for capital expenditures, probably street improvements. Windsor Locks is skeptical of the program's future and is proceeding very cautiously.

(9) Chicopee, Massachusetts, (pop. 66,676), estimates that two-thirds of its funds will be required to stabilize property taxes. A tax increase would have been necessary but for the assistance provided by the revenue sharing program. The remaining amount will be used for capital expenditures in the public safety, environmental protection, and public transportation areas.

(10) Manchester, Connecticut, (pop. 47,994), intends to use its funds for revitalizing the main shopping area of town. This will be done by spending the money for highway and sidewalk construction. Manchester feels that improving both pedestrian and automobile traffic flow to the shopping area will yield long range business and tax benefits to the town.

(11) Granby, Connecticut, (pop. 6,150), has invested its money in a trust fund at 5 3/4% interest for a period of one year. The town expects to spend the money on a library, an additional patrolman, and radio equipment for police cars and town trucks, but wants to wait a year before making a firm decision. There is uncertainty concerning the genuine purposes of the program, and Granby is in no hurry to commit itself.

(12) Simsbury, Connecticut, (pop. 17,475), is departing from the standards followed by most other towns and is planning to use its money for other than capital expenditures or tax reduction. Simsbury's money will be spent

to enlarge the police department staff, the highway department, and to hire a new finance director. Some of the money will probably be spent for road improvements as well, but most of it is going for programs that will require continuous funding, whether or not revenue sharing is extended after five years.

(13) Torrington, Connecticit, (pop. 31,952), will use its money for capital expenditures already planned. Revenue sharing funds will enable the town to speed up the completion of these programs, which include a new garage, bridge and highway repairs, and extension of storm and sanitary sewer systems.

(14) Brattleboro, Vermont, (pop. 12,239) is using its money for an unusual purpose. The city is required by a recent state law to change to a fiscal year accounting system (July 1 - June 30) no later than July 1, 1977. The first budget under the new system must cover 18 months rather than the normal 12. Therefore, Brattleboro plans to shift to the new system in July of this year and use its revenue sharing funds to support the additional six months of the budget.

(15) Woodstock, Vermont, (pop. 2,608), will use its funds for the construction of a new fire station.

(16) Concord, New Hampshire, (pop. 30,022), plans to use its money for capital expenditures already planned. There will be no new programs. Without revenue sharing funds a tax increase would have been necessary.

(17) East Hartford, Connecticut, (pop. 57,583), admits to having no real need for revenue sharing funds. This city has a lot of heavy industry that provides substantial tax revenues to the community. Property taxes in East Hartford are lower than most of the state. The city has not made specific plans for the use of its money, but will probably use it for improvements in the police and fire departments. A tax reduction of 3-5 mills is also planned.

(18) New Haven, Connecticut, (pop. 137,707) is worried that cuts in other Federal programs are going to be made. New Haven needs the funds badly, but is making no plans for their expenditure until the extent of cuts in other programs is known. There will definitely be no tax cut.

(19) Wethersfield, Connecticut, (pop. 26,662), feels that the revenue sharing program does not deserve all the favorable publicity it has been receiving. The Town Manager believes that the regulations governing the program will continue to grow. Wethersfield will use its money to stabilize taxes, primarily by paying for capital expenditures already planned.

(20) Aurora, Colorado, (pop. 74,974), plans to spend its money to remodel a public golf course.

(21) Glenarden, Maryland, (pop. 4,447), intends to use its funds to expand the town hall to hold larger crowds at the weekend cabaret dances held there.

(22) Laurel, Maryland, (pop. 10,525), is planning on using some of its money to buy the old National Guard Armory in the city and turn it into a recreation center.

(23) Bowie, Maryland, (pop. 35,028), will use its share for capital expenditures, primarily for road improvements.

Intended Uses of Revenue Sharing Funds by States

As discussed elsewhere in this paper, most of the state governments have projected surpluses for the current fiscal year, and many have huge surpluses to look forward to. Revenue sharing funds are therefore not as crucial to financial planning by the state governments as for the local governments.

Local governments are prohibited by the 1972 Act from using revenue sharing funds for educational purposes, but state governments have no such restriction. Several states, including California, New Jersey, Oregon, Pennsylvania, and Virginia will use the majority of their revenue sharing funds to assist the local governments in upgrading the school systems.[1] Governor

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[1] "The Fiscal Forecast is Fine for the States," Business Week, February 17, 1973, p. 63.

Tom McCall of Oregon will submit a plan to the state legislature that will completely revise the school financial structure such that the state provides 100 percent of the operating costs of elementary and secondary schools. Revenue sharing funds will be directed toward this goal, with a substantial decrease expected in local property taxes.[1]

Several other states plan on using their money to help lower the property taxes at the local level. In some cases property tax reductions will result from increased state aid to education, in Oregon for example. Other states will use their revenue sharing funds in a more direct manner to permit reduction of property taxes. South Dakota intends to fund a major reform of the state and local tax structure with its share. Illinois, Kansas, Maryland, Minnesota, Vermont, Washington, Wisconsin, and California all have some form of direct funding to local governments to allow a property tax cut.[2]

Some states, to be sure, will use their funds to embark upon new programs. Montana will finance capital projects authorized by the state legislature, but for which the bonding program was voided by the courts. Louisiana plans to use its revenue to finance an expanded highway construction and maintenance program. South Carolina expects to effect major expansions in the fields of health care, criminal justice, and education with its revenue sharing funds. Tennessee will make innovations in

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[1] Ibid.

[2] Ibid.

the areas of early childhood development, including statewide kindergartens which the state does not presently have, mental health, and correctional institutions.[1]

In summary, state governments are expected to use their funds to improve the school systems, finance local property tax reductions, and establish new social welfare programs. In general, the states are not using their funds for direct capital expenditures.

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[1] Ibid.

CHAPTER VII

A CRITICAL ANALYSIS OF REVENUE SHARING

The proponents of Federal revenue sharing have based their support of this program on the following propositions, among others:[1]

(1) That state and local governments face a common fiscal crisis, that they are financially unable to provide the services required of them, and that they have only limited recourse to raise additional funds at their level. The states have exhausted the sources of revenue available to them, particularly since the Federal government has preempted the major source of revenue, the income tax.

(2) That revenue sharing is an equitable method of raising money to meet state and local needs and is an efficient method for meeting public expenditure requirements at these levels.

(3) That additional sources of revenue are necessary for state and local governments because the need for funds at these levels will grow more rapidly than revenue in the future.

(4) That revenue sharing will help restore traditional American democratic principles by returning more power and

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[1] Legislative Reference Service, op. cit., pp. 20-36.

authority to the lower echelon governments. Revenue sharing will not only expand the activities of the state and local governments, but will contribute to the equally desirable goal of retarding the growth of the Federal government.

(5) That states will have practically no restrictions on the use of shared funds, and that local governments, while having more restrictions than the state governments, will still have considerable leeway in the expenditure of shared funds.

(6) That the Federal government is assuming only a limited financial obligation for a limited period of time (five years).

(7) That this program can be administered with very little growth in the Federal bureaucracy and with the imposition of only a few administrative procedures on the recipient governments.

(8) That there is little alternative to revenue sharing if local governments are to continue as a viable part of our governmental structure.

(9) That funds made available to state and local governments are designed to encourage them to expand their revenue efforts, either by greater use of income taxes or other revenue sources. In other words, the bill helps the state and local governments to help themselves.

The above propositions will each be examined and discussed

in order to assess the validity of the assumptions on which they are based.

<u>The Fiscal Crisis of State and Local Governments</u>

The Revenue Sharing Act of 1972 is based on the assumption that all states and localities face a common fiscal crisis. <u>Some</u> states and localities clearly are confronted by a crisis of this type, despite a high tax burden on their citizens; but on the other hand, many localities have not exhausted their own resources or even strained themselves. For example, six states have no income tax whatsoever, four others use it in a narrowly selective way, and in Fiscal Year 1971, individual income tax collections represented less than one percent of personal income in 22 states.[1] State and local officials quite naturally prefer obtaining "free" funds from Washington rather than face their constituencies on the issue of taxes.

The financial situations of the various state and local governments vary so enormously that it is very difficult to generalize. The most accurate generalization, however, must surely be that the potential sources of revenue available to these governments have <u>not</u> been exhausted. It was pointed out above that the state income tax has not been virogously applied by most states. Viewing the state income tax from a slightly

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[1] H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Ways and Means, U.S. House of Representatives, <u>Report with Supplemental, Additional, and Dissenting Views</u> (to Accompany H.R. 14370), p. 85.

different perspective, despite the claim that the Federal government has preempted this major source of revenue, six states (Hawaii, Minnesota, New York, North Dakota, Oregon, and Wisconsin) currently derive a considerable proportion of their total revenues from this source. The other 44 states fall far below this level, imposing a very low rate of taxation or not utilizing the state income tax at all.[1]

Other taxation measures also remain unexploited. Five states (Alaska, Delaware, Montana, New Hampshire, and Oregon) have no general sales tax, and of the others that do, the rate exceeds 4% in only seven states.[2] Six states (Nevada, New Hampshire, Ohio, Texas, Washington, and Wyoming) do not impose a corporate income tax, and the taxation rate is very low in many of the states that do employ it.[3] Although property is taxed by all local governments, the rates are several times higher in some states than in others.

There is no intent to claim that the tax systems and bases of all the 50 states should be the same, but the tremendous variation that exists are difficult to justify. The inescapable conclusion is that the states differ greatly not only in their taxation effort, but also in their willingness to meet

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[1]U.S. Bureau of the Census, Statistical Abstract of the United States: 1972, (93rd Edition), Washington, D.C.: 1972, pp. 412-413.

[2]Newspaper Enterprise Association, Inc., The 1973 World Almanac and Book of Facts, Newspaper Enterprise Association, Inc., New York, 1973, pp. 107-108.

[3]Ibid., p. 115.

their own social obligations. It seems clear beyond doubt that the majority of the states could increase their revenues substantially by requiring the same sacrifices from their citizens as a few conscientious states are doing, rather than waiting for the Federal government to come along and solve their problems.

Some states have, in fact, recently taken steps to exploit these additional sources of revenue. Florida has a projected surplus of $300 million for 1973 due to its newly adopted corporate income tax, and within the last two years Ohio and Pennsylvania joined the ranks of those states having state income taxes.[1] States have long been reluctant to impose personal and corporate income taxes for fear that new industry will be discouraged by states that do adopt these measures. These states should realize that it is not enough for an industry to simply bring jobs to a community, though this is certainly an important consideration. An industry should also contribute to the community by direct taxation. Most communities would be better off not having the industry if significant tax incentives must be offered in order to attract the industry in the first place.

Industries, like individuals, require services from the community, and like individuals, should be taxed to defray the expenses for these services.

Equity of Revenue Sharing

From the previous discussion of varying tax policies

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[1] "The Fiscal Forecast is Fine for the States," Business Week, February 17, 1973, p. 68.

of the different state and local governments, it is apparent that individuals in the same income bracket are taxed differently depending on their domiciles. Even though revenue sharing has certain income redistribution features, the bill places great emphasis on the tax efforts of state and local governments, and encourages the maintenance of high taxes. Therefore, the existing inequity is likely to be perpetuated. The major point is that our present system of taxation treats people in the same income bracket differently simply because they live in different places, and revenue sharing does little to redress these inequities.

Revenue sharing as an efficient method for meeting public expenditure requirements at the state and local level can be directly challenged on the basis that it will help perpetuate the existing inefficient structure of many local governments. The problems of many local governments can be traced to the fact that there is duplication of many services among various units of government. Governments often overlap one another to the extent that several different levels may tax the same parcel of property.[1] Their broadly divergent power and functions have frequently led to unnecessary conflicts and competition. Not only will revenue sharing help perpetuate this situation, but will

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[1] H.R. 14370, 92nd Cong., 2d Sess. (1972): Committee on Ways and Means, U.S. House of Representatives, <u>Report with Supplemental, Additional, and Dissenting Views</u> (to Accompany H.R. 14370), p. 95.

actually make it worse for this reason: since assistance under revenue sharing is provided to every unit of local government, except those whose share is computed to be less than $200, small hamlets will be encouraged to incorporate and share in the Federal bounty. Instead of maintaining the existing fragmented and overlapping governments, and indeed aggravating the problem, pressures are needed to move local governments toward more cohesive, efficient units.

Need for Funds at State and Local Levels

Supporters of revenue sharing have frequently stated that the need for funds at the state and local levels will grow more rapidly than revenues in the future.[1] For quite a long time, especially during the late Fifties and most of the Sixties, this was in fact the situation. The basic fallacy in assuming that this will continue in the future lies in extrapolating the trends of the past decade over the decade ahead, without making the appropriate adjustments to reflect the changing society.[2]

From the mid-Fifties to the mid-Sixties several important factors promoted a huge expansion of expenditures at the state and local level. First, there was a backlog of requirements

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[1] Melville J. Umler, "The Elementary Errors of Tax-Sharing," Revenue Sharing and Its Alternatives: What Future for Fiscal Federalism?, Report, 90th Cong., 1st Sess., (1967); prepared for the Subcommittee on Fiscal Policy of the U.S. Congress, Joint Economic Committee, Washington, D.C.: Government Printing Office, 1967, p. 931.

[2] Ibid., p. 932.

for public facilities left over from the deprivations caused by World War II. Secondly, the postwar "baby boom" resulted in increasing school enrollments. At the same time, advances in medical science and the adoption of health and welfare services caused the number of older citizens in the population to increase substantially.[1] These conditions that created the great demand for public facilities are due to change significantly during the next decade.

The backlog of needs from World War II has long since been fulfilled. The birthrate in the U.S. reached its peak in the late Fifties, and has declined to the point that today we have almost reached "Zero Population Growth." In many areas the enrollment in public schools has already started to decrease. The "war babies" are now adults. The decline in school enrollments will become even more marked as the results of our present low birth rate begin to be felt in the next few years. Additionally, the number of older citizens as a percentage of the population has stabilized.[2] This, together with the increased support of the older citizens provided by recent increases in Social Security and the adoption of Medicare, should ease the demand for increased services from local units of government.

As a result of all these factors, expenditures required to maintain the present scope of public services at the state and local levels should rise by a much smaller amount in the

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[1] _Ibid._, p. 933.

[2] Melville J. Ulmer, op. cit., p. 933.

next decade than in the past decade. In summary, it appears that revenue sharing is a concept whose time has passed; but ironically, it was adopted just as the future began to brighten for state and local governments. In 1967 the Committee for Economic Development estimated that the required outlays by state and local governments for public services in 1975 would be $98.5 billion. From 1955 to 1965, state and local expenditures had increased by 123 percent.[1]

At the same time, the Committee for Economic Development projected the net revenue yield to state and local governments, from the existing tax structure, at $119 billion in 1975, a figure far in excess of the projected requirements. As a matter of fact, in 1969 the revenues realized by state and local governments amounted to $114.5 billion.[2]

The most recent information available concerning the fiscal situation of state governments paints a rosy picture for the future. Governor Ronald Regan of California was recently quoted as saying that his state's budget outlook is "brighter than it has been in years," and Governor Nelson Rockefeller of New York declared that his state has "weathered the severe fiscal crisis which beset us for the past two years."[3]

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[1] Melville J. Ulmer. op. cit., p. 933.

[2] U.S. Bureau of the Census, Statistical Abstract of the United States: 1971, (92nd edition) Washington, D.C., 1971, p. 406.

[3] "The Fiscal Forecast is Fine for the States," Business Week, February 17, 1973, p. 68.

In a majority of the states there are budgetary balances or surpluses for the foreseeable future, few new state taxes, and in some states, even tax cuts. The following examples serve to illustrate the healthy fiscal situation of the state governments:[1]

(1) Florida will have a surplus on the order of $300 million, due primarily to the long-overdue adoption of a corporate income tax.

(2) Michigan is expecting a surplus of around $220 million for the current fiscal year. Governor Millken has proposed tax cuts for both individuals and corporations for the next two fiscal years.

(3) Pennsylvania is also sufficiently liquid to be considering a tax reduction for both individuals and corporations.

(4) Connecticut's budget for the current fiscal year provided for a small surplus, while at the same time reducing the sales tax from 7% to 6.5% and repealing some business taxes.

(5) Mississippi has an $80 million surplus of which at least part will be distributed to local governments within the state.

(6) Georgia will use its $50 million surplus to either reduce property taxes or boost state aid to schools.

(7) California expects a whopping $850 million surplus for the current fiscal year, and possibly $1.2 billion in the next. The governor wants to return most of the surplus to taxpayers, whereas the legislators want to use the money for other purposes.

(8) New York has a projected surplus of $75 million for the current year and wants to put $66 million of this in a contingency fund, a plan that has brought charges of political opportunism for the gubernatorial campaign next year.

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[1] Ibid.

(9) Texas, a state with no corporate or personal income tax, will have a surplus of $50 million this year, due primarily to higher sales and excise taxes.

There are some states, to be sure, that are finding it difficult to meet budgetary demands at present, and a few may actually have to increase taxes. The fact remains, however, that state governments in the aggregate had a surplus of $12.3 billion at the end of 1972, including $2.65 billion from revenue sharing.[1] This clearly indicates the ability of state governments not only to solve their own problems, but to assist the local governments within the states. For example, the State of Michigan with its substantial surplus should use some if its funds to assist financially-distressed Detroit. This city is in such poor financial condition that its schools may have to close two months early due to lack of funds.[2] Even so, the state of Michigan appears to be oblivious to this situation, and plans on cutting taxes rather than developing a plan to aid some of its own cities and communities.

This discussion has dealt with revenues and expenditures in the aggregate, and it cannot be denied that <u>some</u> local governments will continue to experience fiscal difficulties. However, there is ample evidence that the severest financial trials of state and local governments have now been ameliorated to the extent that these problems can be solved in the overwhelming majority of cases by the fiscal measures available to these governmental units.

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[1] *Ibid.* [2] *Ibid.*

Restoration of Power and Authority to the Lower Echelon Governments

President Nixon has repeatedly voiced his belief that a "New Federalism" is needed to bring governmental operations closer to the people served thereby, and that a system of revenue sharing will result in both power and money being returned to the governmental units closest to the people. Unfortunately, it is no simple matter to reverse the course of events over the past century, and especially the last fifty years.

The role of the Federal government has expanded enormously during this period of time due to several important factors. One of these is the historic, inexorable trend toward greater economic interdependence of American society that transcends city, county, and state boundaries. The population is so mobile that the very concept of residents of a state begins to lose meaning. The services provided by one affects all its neighbors. In short, population mobility, industrialization, and the advances in transportation and communications have molded the nation into a cohesive whole. These historical trends are not reversible, and the likelihood is that the Federal government will grow stronger, not weaker. The flow of a few billion dollars to the state and local governments, along with wide latitude for their expenditure, will not alter the existing power relationships between Federal, state, and local governments.

The American society will continue to be molded by Federal leadership. In providing minimum social and economic

standards for American society, the states have always been led by the Federal government. There are many examples, but the Civil Rights Act of 1964 readily comes to mind as an action by the Federal government to alter longstanding social and economic conditions existing in the various states. The Federal government has pioneered other social legislation with the inevitable economic consequences.

The basic reason why many states have always lagged, and will always lag, in adopting progressive legislation has to do with the competition among the states for industry, a problem previously alluded to.[1] Some aspects of this competition are socially unhealthy and economically self-defeating when industry is lured to a state by sacrificing the welfare and best interests of the state's own people. For example, a state may decline to impose regulations on industry for limiting air or water pollution for fear of conceding an advantage to another state in attracting new industry. All states are better off if the Federal government adopts legislation imposing a general pollution standard that does not weaken any one state's competitive posture for attracting industry. In summary, the Federal government has done for the states what they themselves were unwilling or unable to do, and by and large this has been for the betterment of American society. Revenue sharing cannot, and indeed _should not_, curtail the power and authority of the Federal government.

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[1] Melville J. Umler. op. cit., p. 935.

One final point regarding governmental authority and responsibility should be made. Public accountability is severly undermined by a bill which divorces the responsibility for raising taxes from the dispensation of public benefits. This is a serious defect, because the public will be unable to measure the performance of their elected officials at various governmental levels by balancing the tax burdens imposed by these officials against the public benefits they have provided.[1]

Restrictions on the Use of Revenue Sharing Funds

The Revenue Sharing Act of 1972 places practically no restrictions on the use of funds by state governments, and establishes certain categories of expenditures for which local governments may use their funds. State governments can apparently be trusted, whereas local governments apparently cannot be. This is the ultimate paradox of the revenue sharing bill: legislation purporting to revitalize local government and return power to the level of government closest to the people actually expresses the least confidence in the wisdom and responsibility of the government at that level.

The restrictions that are placed on the expenditure of funds bear the mark of a typical Congressional compromise. The Senate version of the bill placed no restrictions on either the state or local governments, whereas the House version would have

[1] H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Ways and Means, U.S. House of Representatives, Report with Supplemental, Additional, and Dissenting Views (to Accompany H.R. 14370), p. 89.

placed firm restrictions on both. The ensuing compromise contained elements of each version.

The present restrictions on local governments are somewhat loose and allow considerable room for maneuver by innovative officials, but it should surprise no one if tighter and more pervasive restrictions eventually ensue, assuming that revenue sharing is extended beyond its present five-year life. If past experience is any indication, there can be little doubt that the dependence of state and local governments on Federal largesse to meet their basic governmental responsibilities will result in the Federal government eventually prescribing how these governments must meet their responsibilities.

Federal Obligation

The proponents of revenue sharing have emphasized that the Federal government is assuming a limited obligation for a limited period of time.[1] Though the President originally envisioned a permanent program, it now seems likely that various political forces will not want it extended after five years. However, the same political pressures from lower levels of government that forced Congressional support of the bill in the first place, may make it difficult to let the program die after 1976, especially during the period of a major election campaign. The program may well prove to be permanent and ever rising in its cost.

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[1] *Ibid.*, p. 2.

Even before the first checks were distributed, important officials were already decrying the inadequacy of the annual funds to be shared. Governor Nelson Rockefeller of New York, testifying before the House Ways and Means Committee on behalf of the National Governors' Conference, recommended that the annual payment be doubled. Ten billion dollars "is absolutely essential," he declared.[1] In short, the same pressures responsible for the present bill will insure rapid growth of the program to meet the insatiable appetites of officials for revenues they can use to finance benefits without the painful necessity of imposing taxes.

Program Administration

The revenue sharing program envisions an administrative situation that can be handled with little growth in the Federal bureaucracy and with the imposition of only a few administrative procedures. If revenue sharing becomes a permanent program, it seems highly probable that it will be accompanied by a burgeoning bureaucracy. It is true that the program as presently constituted takes advantage of existing facilities and personnel levels of the Treasury Department to a large extent, but it must be remembered that the program is in its infancy. The first round of reports have not yet been received from governmental units benefiting from revenue sharing. With approximately 39,000

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[1] *Ibid.*, p. 95.

different governments already participating in the program, it is inconceivable that there will not be a deluge of problems to be solved by the "experts" in Washington, D.C. There are thousands of additional units of government in the country who are potential participants in the program. Who is going to work out the problems concerning their eligibility for funds, their late entrance into the program, the effect it would have on funds received by the presently participating governments, etc? There can be little doubt that this program, like all other governmental programs will experience growing pains, and the prescription for those pains will inevitably involve additional manpower and facilities, bureaucracy, if you will.

Alternatives to Revenue Sharing

Revenue sharing has often been presented as the only remaining hope for the salvation of our state and local governments. It has already been pointed out in the discussion on taxes that most state and local governments are not even in need of salvation. And in those few situations where some assistance is required to allow governments at this level to function effectively, there are other methods to achieve this goal with greater efficiency and a lesser expenditure of funds.

It is completely unjustifiable to dispense funds to all units of government, as the present program does, simply because a small minority of them require assistance. However, there is

no easy solution to providing selective assistance simply because of political considerations. Any method that could be devised would be opposed by some powerful interest groups. An interesting analysis of alternative ways of distributing Federal funds was conducted by the Advisory Commission on Intergovernmental Relations (ACIR) in 1964. This commission, composed of representatives from the three levels of government, Federal, state, and local, was created by Congress in 1959 for the following purposes:[1]

> (1) To give critical attention to the conditions and controls involved in the administration of Federal grant programs.
>
> (2) To recommend within the framework of the Constitution, most desirable allocation of governmental functions, responsibilities, and revenues among the several levels of government.
>
> (3) To recommend methods of coordinating and simplifying tax laws and administrative practices to achieve a more orderly and less competitive fiscal relationship between the levels of government.

The ACIR analyzed the following alternatives for distributing Federal funds:[2] (1) The compensatory fiscal approach, which would involve reduction in the Federal income tax, with the state and local governments presumably realizing the

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[1] Richard F. Kaufman, "Recommendations of the Advisory Commission on Intergovernmental Relations and Earlier Government Commissions," Revenue Sharing and Its Alternatives: What Future for Fiscal Federalism? Report, 90th Cong., 1st Sess., 1967, prepared for the Subcommittee on Fiscal Policy of the U.S. Congress, Joint Economic Committee, Washington, D.C.: Government Printing Office, 1967, p. 210.

[2] Ibid., pp. 210-245.

opportunity to raise their own taxes, (2) the tax credit option approach under which a more genersous write-off of state and local taxes toward payment of Federal income taxes is permitted, again with the intent of providing an opportunity to raise state and local taxes, (3) the tax sharing approach, a variation of the revenue sharing approach that was eventually adopted. Under this plan a designated percentage of Federal tax revenue would be distributed to the states on the basis of collection, (4) the unconditional grant approach under which the states would be left free to allocate the funds as they deemed best, (5) the conditional grant approach under which the Federal government would decide on the function to be financed, and (6) the direct federal expenditure approach under which the Federal government would not only decide on the function to be financed, but expend the money directly with no matching funds or participation from the state and local governments.

The advantages and disadvantages of these various approaches and the political considerations thereof will not be discussed in any detail here. Suffice it to say that while it did not reject the concept of revenue sharing, the ACIR felt that other approaches should first be tried, with revenue sharing to be considered only if the other methods prove ineffective.[1] In particular, ACIR gave strong support for the tax credit proposal and the Federal grant system, both conditional and unconditional. It emphasized

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[1]*Ibid.*, pp. 244-245.

that grants should be consolidated to achieve more efficiency and eliminate fragmented programs, and most importantly, to reflect differences in the states' relative fiscal capacities. ACIR also placed importance on maintaining the relation between taxing and spending responsibilities at the local level, and in this regard took the position that fiscal reform by local governments would give them additional funds by making more effective use of their own taxing powers.

It can be seen, therefore, that alternatives to revenue sharing do exist that would put the money where the necessity can be demonstrated, but would not distribute funds to every unit of government. At the same time, efficiency on the part of local governments would be encouraged and the concept of responsibility and accountability to the people would be maintained.

Expansion of Taxation Efforts by State and Local Governments

As we have seen, the state income tax is not being used to the maximum extent possible in most areas. The increased use of it is an avowed goal of revenue sharing. This highlights another paradox of the revenue sharing program. On the one hand it is claimed that most states are in desperate need of assistance from the Federal government. On the other hand, the government explicitly recognizes the ability of the state

governments to raise substantial additional revenues without placing an undue burden on the population of the state. The "piggyback" collection provision of the 1972 act expressly acknowledges that state governments are not doing enough to solve their own problems.

The revenue sharing bill also is designed to encourage additional taxation effort at the local level. This was pointed out in the discussion of the "three-factor formula" and the "five-factor formula" in Chapter V. Since the major source of revenue at the local level derives from the property tax, the bill implicitly encourages maintenance of taxation effort in this area. This is in direct conflict with one of the goals of revenue sharing frequently expressed by President Nixon, that of providing relief from property taxes at the local level.

The revenue sharing program abounds with paradoxes and inconsistencies. Revenue sharing was enacted at a time when state governments were finally moving toward long needed change to solve the problems of local governments within those states. In the area of education, for example, an area that consumes 43 percent of local budgets and in which 95 percent of the local tax revenue for education is derived from property taxes, several state courts (including California, Texas, Minnesota, and New Jersey) have issued decisions that may require states to provide nearly all the costs of public education.[1] Presumably this would

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[1] H.R. 14370, 92nd Cong., 2d Sess. (1972); Committee on Ways and Means, U.S. House of Representatives, Report with Supplemental, Additional, and Dissenting Views (to Accompany H.R. 14370), p. 106.

have to be accomplished through a state income tax, since the rulings explicitly stated that linking education to property taxes discriminated against the poorer area. Why not let the state courts complete its work in this regard? It is reasonable to believe that the states could support public schools through an income tax, with local governments utilizing the property tax to provide other services.

CHAPTER VIII

CONCLUSIONS

As finally enacted into law under the State and Local Fiscal Assistance Act of 1972, revenue sharing emerged as a type of "pork barrel" program designed to give maximum political benefit to Senators and Representatives in Congress. The case for revenue sharing was built on several erroneous assumptions, the most important being that most state and local governments are in serious financial straits, and further, that they do not have the fiscal resources at their disposal for solving their own problems.

Based on the limited number of personal interviews conducted with officials of local governments, there appears to be little urgency in expending the funds received through the new revenue sharing program. Various newspaper and magazine articles tend to substantiate the belief that while revenue sharing funds are gleefully accepted by state and local governments, as one would expect, there is nothing to indicate that revenue sharing was necessary, in the vast majority of cases, for the continued viability of the recipient governments.

Revenue sharing as first proposed in the early 1960's and as reflected in President Nixon's first proposal to Congress

in 1969, was based on the concept of sharing <u>surplus</u> revenues with state and local governments on the basis of population and the degree to which their own tax resources were being utilized. When it became apparent that there was little chance of having any surpluses to share, Mr. Nixon embraced revenue sharing as part of a deficit budget, but hoped to use this program as a vehicle for consolidating the grant-in-aid programs under the special revenue sharing aspect of his plan.

The resulting program contained the worst of both worlds. A nationwide expectation had arisen, largely due to the intense lobbying and public activity on the part of organizations of state and local officials, whereby manna from Washington would flow to every community to enhance its lot without cost to anyone. The very apt economist's homily, "there is no such thing as a free lunch," was completely ignored in the great clamor for Washington to dispense its presumably endless largesse. As a result, a program was adopted for the debt-ridden Federal government to distribute $30 billion over a period of five years to lower government which are by-and-large in much stronger fiscal condition than is Washington. Additionally, no economies in other areas were realized, as the President had hoped. No substantial incentives were adopted to make state and local governments more effective and no restructuring of the many overlapping governmental functions was achieved. In short, everything is

the same as before, except that the Federal government is further in debt.

State and local officials are happy to receive the money, of course, but if they had the will and the wisdom to look at the nationwide affects of revenue sharing, taking into consideration both sides of the ledger, there can be little doubt that in the aggregate, the country is worse off for having adopted this program. The only way it could have improved the condition of the entire country would have been through the reorganization of inefficient units of government or by an overhaul of the tax structure. The Act of 1972 does neither.

Some mileage from revenue sharing may yet be obtained by President Nixon. Though it was not in the original scheme of things, it appears now that the President may use revenue sharing as an excuse for cutting back on other programs. Mr. Nixon has received much publicity recently for his proposed dismantlement of many "Great Society" programs adopted in the 1960's. The Administration could always point to revenue sharing as a means for local governments to continue some of the programs for which funds are terminated. There have already been hints from Administration spokesmen that revenue sharing may be used to ease the way for cutbacks in other areas.

The Research Questions

In response to the primary research question, the information gathered for this paper leads to the conclusion that

Federal revenue sharing will help maintain the status quo of taxation policies of state and local governments, at least for the five-year life established under the initial legislation. If revenue sharing becomes a permanent program after this trial period, tax policies might change substantially.

This conclusion is based primarily on the following factors:

(1) Many local governments that could afford to reduce taxes as a result of revenue sharing are not doing so for fear that the program may be terminated after five years, necessitating a tax increase at that time. Most officials feel that the public is not clamoring for a tax reduction and will remain satisfied if taxes are kept at the present level.

(2) Most officials interviewed asserted that a tax increase would have been necessary if revenue sharing had not been adopted when it was. While this is probably exaggerated in some cases, it does indicate that tax levels in most states and communities will remain at the present level.

(3) While the 1972 Act does contain an incentive for the increased tax effort of state and local government, the incentive is not all that strong. For one thing, the choice of two formulas for distribution of funds allows those states without income taxes to choose the "three-factor formula" that does not penalize them. For another, even though both formulas contain a General Tax Effort Factor to reward those states collecting a higher per capita tax, this factor is not strong enough in relation to other factors to encourage governments to take the political risky step of increasing taxes. Lastly, it is incongruous for the Federal government to adopt a law that ostensibly encourages additional tax effort by state and local governments, and at the same time provides money that obviates the need for the tax effort that has been encouraged.

The "piggyback" income tax collection feature of the Revenue Sharing Bill is not likely to stimulate additional use

of the state income tax. None of the states without an income tax are experiencing fiscal deficits at the present time. Moreover, in a preponderance of the states the budgetary outlook for the 1973 legislative session is brighter than it has been in years. Unless some of the states decide to adopt a revenue sharing plan of their own for distribution of state funds to local governments, an extremely unlikely event in view of the Federal revenue sharing program, there should be no need for increases in state income taxes. Some states may, however, choose to utilize the services of the Federal government in collecting state income taxes as provided by the "piggyback" feature, while retaining the present level of taxation.

In short, state and local governments (in the vast majority of cases) are experiencing the combined blessings of a resurgent economy, a leveling off of demands for services from the older segment of the population, a decrease in school enrollment, and "free" funds from Washington in the amount of $30 billion over a five year period. There is little reason to alter taxation policies for the foreseeable future.

During the Congressional legislative process, the revenue sharing concept evolved as follows:

(1) From a proposal to share surplus revenues, initially in the amount of about $500 million per year, to a massive program of assistance without regard to budgetary deficits, with $5.3 billion available the first year.

(2) From a proposal to channel all shared revenues through the state governments, with the state government retaining

more than half, to a system of direct grants from the Federal government to each unit of lower government, with state governments receiving one-third and local governments receiving two-thirds.

(3) From a relatively simple allocation plan wherein money would be distributed on the basis of population and tax effort, to a dual system of complex plans under which the factors of need, use of state income tax, and urbanized population are used in addition to overall population and overall tax effort.

(4) From a plan granting funds to all units of government without "strings," to a compromise plan under which the states have no restrictions, but under which local governments must use their money for certain priority categories of expenditures.

(5) From a plan that envisioned the sharing of a certain percentage of Federal revenues over an indefinite period of time, to one under which specific dollar amounts were appropriated over a specified period of time.

(6) From a plan that favored rural areas to one that favors everyone, due to the two allocation formulas available. In reality, suburban areas are not particularly favored by either of the formulas, whereas rural areas and core cities both are, depending on the formula selection.

All the changes discussed in the preceding paragraph entailed political trade-offs and compromises between the executive and legislative branches, and between various factions of the Congress. In general, the House advocated features that would benefit the more populous urban regions, while the Senate had the more rural interests at heart. Also, the House advocated tight restrictions on the use of funds, whereas the Senate was inclined to grant funds without restriction on their usage. The House fought vigorously to include incentives for the use of state income taxes, while the Senate objected to this goal and managed to water-down this provision considerably.

There were some points of unanimity between the House and Senate, however. Both favored direct distribution of funds to each unit of government, rather than granting the state governments control over funds earmarked for local governments, as the President had proposed. Additionally, both agreed that local governments should receive the majority of the money, whereas the President's plan would have granted the majority to the state governments. The House and Senate both employed similar procedures to avoid giving control of the legislation to the House and Senate Appropriations Committees and to avoid the necessity for annual appropriations procedures.

Additionally, both the House and the Senate refused to consider what was probably the most intelligent and farsighted proposal made during the whole legislative process: the provision of the aborted Humphrey-Reuss plan of 1971 that would have required state and local governments to enact master plans for modernization prior to participating in revenue sharing. If the final revenue sharing legislation <u>had</u> contained a provision for modernization of local governments to eliminate some of the overlapping functions, perhaps it would have been worth the $30 billion that is to be handed out.

The revenue sharing program appears to be functioning well insofar as the administration of the program is concerned. A series of regional meetings has been conducted by the Office of Revenue Sharing to acquaint officials of state and local

governments with the regulations and procedures established by the 1972 Act. Officials interviewed seemed to be well informed concerning their responsibilities under the act. The machinery established to administer the program is viewed favorably by these officials, and the amount of governmental "red tape" has been held to a minimum.

It is quite clear that the local governments are using their revenue sharing funds for projects of limited duration or for capital expenditures, i.e., for programs that will not require funding over a long period of time. There is considerable doubt in the minds of the mayors and city managers that revenue sharing will be extended after the initial five-year period. They are "playing it safe" and planning expenditures in such a way that taxation can be kept at the present level. Revenue sharing has therefore enabled governmental units to buy new equipment, erect new buildings, or pave new streets, all projects that would otherwise have not been accomplished. Many governments have used funds for projects that clearly are not "must" items. The most flagrant example is probably the city that is using its money to renovate the golf course.

In general, revenue sharing has permitted communities to purchase "nice to have" projects, but few seem to have needed the money for "absolutely essential" projects.

COMPARISON OF FOUR REVENUE SHARING PROPOSALS

	NEW NIXON PROPOSAL	HUMPHREY-REUSS PLAN	MUSKIE PROPOSAL	MILLS PLAN
Amount and Appropriation	$5 billion for general revenue sharing in fiscal year 1972 (1.3 percent of taxable personal income). $11 billion ($10 billion in consolidated Federal aid programs plus $1 billion in new funding) for special revenue sharing. Permanent appropriations bill.	$3 billion in fiscal year 1973. $7 billion in fiscal 1974; $9 billion in fiscal 1975. Annual appropriation.	$2.8 billion in fiscal 1971; $3.9 billion in fiscal 1972. (half the sum of 1 percent of taxable personal income and 25 percent of state income tax collections). Permanent appropriation to trust fund. Credit against Federal income tax of 40 percent of state and local income tax paid.	A five-year program to grant fixed annual sums (about $30 billion total; roughly $1 billion more than Nixon's plan). $5.3 billion in fiscal year 1972. Permanent appropriation to a trust fund.
State Allocation	90 percent of $5 billion general revenue sharing funds: percentage of total U.S. population, adjusted to reflect relationship of state tax effort to total state personal income. Remaining 10 percent: if negotiated local sharing formula adopted. $11 billion special revenue sharing: by formulas to be announced.	Same as Nixon proposal, except that no special revenue sharing plans are included.	Population adjusted by relative tax effort.	Population adjusted for need (based on state per capita income as compared to national per capita income), overall tax effort, and use of state income tax. One-third of state's allocation to go to state government.

NEW NIXON PROPOSAL	HUMPHREY-REUSS PLAN	MUSKIE PROPOSAL	MILLS PLAN
Local Allocation	**Local Allocation**	**Local Allocation**	**Local Allocation**
All funds to be channeled through state government. Approximately 50 percent of state share to local governments, according to ratio of local revenues to state revenues, unless negotiated local sharing formula adopted. Individual local shares according to proportion of total local revenues raised unless determined by negotiated formula.	Similar to Nixon proposal. Unless local allocation formula negotiated, passage of state law required distributing local share according to population or revenue raised.	Amount of local pass-through determined by local share formulas. Cities and counties over 100,000 shares based on relative tax effort; 50,000 to 100,000; reduced shares; municipalities under 50,000; determined by state.	Federal government to make determination. Two-thirds of state allocation to local governments. Federal government to deal directly with local governments. Shares based on relative tax effort and need.
Incentives	**Incentives**	**Incentives**	**Incentives**
Additional share of remaining 10 percent to states adopting negotiated distribution formula in agreement with local governments.	Same as Nixon proposal; in addition, an adjustment for state tax effort in allocating state shares, income tax revenue would be weighted double that of other revenue, beginning with fourth year of operation, starting July 1, 1974.	Income tax credit; Federal collection of state income taxes authorized; credit increased for state estate taxes paid.	Total tax effort rewarded. Specifically encourages use of state income tax.

PROPOSAL	PLAN	PROPOSAL	PLAN
Restrictions	Restrictions	Restrictions	Restrictions
Few restrictions. States required to share funds with local governments. Local sharing to be in addition to pre-existing state sharing programs. Anti-discrimination provisions applying to all Federal aid programs apply.	To qualify for sharing in second year, beginning July 1, 1972, state must enact master plans for modernization of state and local government; otherwise similar to Nixon plan.	Similar to Nixon plan.	More control by the Federal government than under Nixon plan. All funds restricted to national high priority needs as determined by the Federal government.

APPENDIX II

SUMMARY OF INTERVIEWS CONDUCTED WITH OFFICIALS OF LOCAL GOVERNMENTS

Gainesville, Florida (population 64,510)
Person interviewed: City Manager, Mr. B. Harold Farmer
Date of interview: December 20, 1972

Gainesville is a rapidly growing city in central Florida that has doubled its population in the last decade. The city is to receive approximately $807,248 in the first two checks, spaced only a month apart. Gainesville intends to use its money for capital improvements and a few programs that will have a limited life and a specific date established for their demise. The intention is to avoid any program that would require funding from local resources in the event revenue sharing is eliminated after the initial five year period.

Mr. Farmer was extremely cordial and helpful, as well as frank and open, during the interview. He stated that his efforts will be directed not only to the wise expenditure of the funds received, but also for building a case for extending revenue sharing beyond the present five year life established by the 1972 Act. He feels this is particularly necessary in that the Congressman representing Gainesville's district did not support the present revenue sharing bill.

Gainesville will not apply any of the funds toward a property tax reduction. The two major reasons for this are that the taxation rate could be reduced only by such a small amount (approximately 3.4 mill) that the individual taxpayer would hardly feel the benefit therefrom, and it is feared that a tax cut now would necessitate a tax increase in five years if revenue sharing is not extended.

Mr. Farmer appeared to be a city manager very much attuned to the times. He stated that a portion of the city's revenue sharing money would be spent to finance a study on bond funding and for a system of program evaluation. He feels that the rules for the expenditure of revenue sharing funds and the administrative procedures involved are easy to comply with, but he is wary of the role that GAO might play. Mr. Farmer also fears that the Federal government might use revenue sharing as an excuse to curtail other assistance such as grants-in-aid.

Alachua County, Florida (population 104,764)
Person interviewed: Coordinator, Office of Federal Aid Programs, Mr. Norm LaCoe
Date of interview: December 20, 1972

Alachua County is the county in which the city of Gainesville is located, Gainesville being the county seat and largest city. Alachua County is one of the few governmental units surveyed that intends to effect an actual tax reduction using revenue sharing funds. Quite a few other units indicated

that revenue sharing had obviated the necessity of imposing higher taxes, but only a few envisioned an actual reduction.

Mr. LaCoe indicated that the tax reduction to be realized was more apparent than real, and that it was politically inspired rather than a matter of sound fiscal policy. About one-third of the revenue sharing funds will go for property tax relief, but the rate of taxation will decline by less than one mill as a result of this action. The tax reduction results primarily from the 1972 elections in which two of the five seats on the Alachua County Commission were to be filled. Both winning candidates had campaigned on the promise to use revenue sharing funds for tax reduction. After taking office, these two candidates were able to persuade a third Commissioner to join them in voting for the tax cut.

Alachua County has not decided on the exact use of the remaining two-thirds of the revenue sharing funds, but it is expected that the money will be spent primarily on capital expenditures, mostly road construction and maintenance.

Huntsville, Alabama (population 137,802)
Person interviewed: Mayor Joseph Davis
Date of interview: December 22, 1972

Huntsville is a city that has experienced phenomenal growth since World War II. Ten years ago the population was about 70,000 and twenty years ago, about 15,000. This growth has resulted in a tremendous expansion of governmental services.

The tax base has also grown accordingly, so the city has been able to cope fairly well with its expansion.

Huntsville has not yet decided how its funds will be used, but there will be no property tax reduction. The city seems to be taking its time before making any definite commitments. In the meantime the money has been deposited in an interest-bearing account, where it will probably remain a year or so before being used.

Hartselle, Alabama (population 7,355)
Person interviewed: Ms. Sarah S. Keseker, City Clerk
Date of interview: December 26, 1972

Hartselle plans to avoid using any funds for programs of a continuing nature. Funds from the first two checks are to be used for street improvement, a new road grader, and a new dump truck.

Mrs. Keseker had recently attended a regional meeting in Atlanta, Georgia, held by officials of the Office of Revenue Sharing, a new division of the Treasury Department. Officials of local governments were advised to proceed on the assumption that revenue sharing would terminate at the end of the first five year period. This seemed to be based on conservative management rather than on any specific information as to the future of revenue sharing. Mrs. Keseker stated that there seems to be a general mood among city and town officials that revenue sharing

will afford a breather for five years, and after that everyone will be on his own.

Decatur, Alabama (population 38,044)
Person interviewed: Mayor Russell Bolding
Date of interview: December 26, 1972

The Mayor said that there was no intention to reduce taxes through the use of revenue sharing funds. Decatur has a very moderate tax rate and there is no clamor by the citizens there to cut taxes using these funds. The money for the first two checks are not to be placed in the general revenues budget, but will be shown as a supplement to the regular budget. The funds are to be used for upgrading presently underfunded departments, primarily in the area of capital expenditures for street improvements, new fire department equipment, and drainage projects. Some of the money, however, will be applied to programs of a continuing nature. The Mayor is wary of funding permanent-type programs with revenue sharing funds, but believes this is necessary to some extent.

Tucson, Arizona (population 262,933)
Person interviewed: Mr. Clifford W. O'key, City Manager
Date of interview: January 3, 1973

Tucson will use all of its revenue sharing funds from the first two checks (about $4,000,000) for the improvement of streets. Pending project design and the awarding of contracts, the money has been invested in a trust fund at 6 percent interest.

The City Manager stated that Tucson would definitely avoid committing revenue sharing funds to programs of a continuing nature. Funds in the remaining four years of the program will be committed to capital expenditures, primarily street improvements and sewage systems. No tax reduction is envisioned. Tucson sees the opportunity to finance street improvements that would have otherwise have been postponed for a long time, and this is considered more pressing than a tax cut.

Sante Fe, New Mexico (population 41,167)
Person interviewed: Mr. Antonio Lopez, City Finance Director
Date of interview: January 4, 1973

Sane Fe is a city with a rather stable population. Its problems are mostly those of an older city, rather than those of a rapidly expanding community. The city has made no definite plans for using its revenue sharing funds, but there will be no tax cut. Programs of a permanent nature will be avoided as much as possible. Sane Fe intends to wait several months before making a decision concerning use of this money. The city wants to be sure that funds from other Federal programs are going to remain intact before it commits itself on the revenue sharing funds.

East Granby, Connecticut (population 3,532)
Person interviewed: Mr. William Meyer, First Selectman
Date of interview: January 19, 1973

East Granby is a small town situated halfway between Hartford and Springfield, Massachusetts. Mr. Meyer stated

that without revenue sharing funds, a local property tax increase would have been necessary. With these funds, the tax rate will be held at the present level, or possibly reduced by about one mill.

The town has plans to use revenue sharing funds for capital expenditures that had already been planned. These include a new truck for road construction, a new police cruiser, and land fill scales for the town dump. East Granby is skeptical about the long range future of the revenue sharing program.

Suffield, Connecticut (population 8,634)
Person interviewed: Mr. Daniel Sullivan, First Selectman
Date of interview: January 19, 1973

Mr. Sullivan also asserted that a tax increase would have been necessary had revenue sharing not been adopted. Taxes will not be reduced, but the anticipated increase will not take place. The town's funds will be used to finance capital expenditures that were already planned. These expenditures include money for a new garage, a drainage system, and partial funding of a new bridge.

Windsor Locks, Connecticut (population 15,080)
Person interviewed: Mrs. Irma M. Olivi, Town Clerk, January 19, 1973

Windsor Locks plans to use about half of its funds for bond reduction, a reflection of the skepticism with which it views the future of revenue sharing. The remaining half will be used for capital expenditures, although the specific programs

have not yet been selected. Mrs. Olivi credits revenue sharing for having stabilized the local tax situation, but states that the town is proceeding on the assumption that this is only a temporary source of funds.

Granby, Connecticut
Person interviewed: Mr. Donald Flannery, Chief Administration Officer
Date interviewed: January 19, 1973

For the time being Granby has invested its money in an interest-bearing trust fund. Plans call for spending the money in about a year. The funds will be used for the purchase of new radio equipment for police and town trucks, addition of another patrolman to the town police force, and partial financing of a new library. Mr. Flannery credits revenue sharing for allowing the town to maintain its present level of property taxation.

Simsbury, Connecticut (population 17,457)
Person interviewed: Mr. Russell Shaw, First Selectman
Date of interview: January 26, 1973

Simsbury is a very affluent town, a suburban commuter area north of Hartford. Simsbury's planned use of revenue sharing funds is in marked contrast to the plans of most officials interviewed. It will use most of its funds to finance new programs of a continuing nature. Very little will be spent on capital improvements and none at all for tax reduction. The new programs to be funded include enlargement of the police department staff, hiring of additional employees for the highway

department, and hiring of a new finance director. These programs will require continuous funding, whether or not revenue sharing is extended after five years.

Torrington, Connecticut (population 31,952)
Person interviewed: Mayor Frederick Daley
Date of interview: January 26, 1973

Mr. Daley plans to use Torrington's money for capital expenditures that were already planned. He states that these programs would have been accomplished eventually anyway, but that revenue sharing has enabled the town to speed up its schedule for completing them. The funds will be used for a new garage, expansion of storm and sanitary sewers, and bridge and highway repairs. No money will be applied toward a tax reduction.

Chicopee, Masachusetts (population 66,676)
Person interviewed: Mr. Norman J. Ritchott, City Auditor
Date of interview: February 2, 1973

Mr. Ritchott explained that without revenue sharing funds the city of Chicopee would have experienced a substantial tax increase. An estimated two-thirds of the funds will go for tax stabilization, and the remainder will be used for capital expenditures in the public safety, environmental protection and public transportation areas.

The city realizes that if revenue sharing is terminated five years from now, there will have to be a property tax increase.

There is some concern that a tax increase may be necessary in the near future if Federal funding of other programs is curtailed, as the rumor-mills suggest.

Manchester, Connecticut (population 47,994)
Person interviewed: Mr. Thomas Moore, Comptroller
Date of interview: February 2, 1973

The city of Manchester is using its revenue sharing funds for an unusual type of investment. There has been increasing concern that the city's shopping area is losing too much business to neighboring towns, especially Hartford, due to its poor accessibility. Therefore, Manchester intends to revitalize the main shopping area by spending its revenue sharing money for new sidewalks and highway improvements. The city feels that improving both automobile and pedestrian access to the shopping areas will yield long range business and tax benefits that make this investment attractive. There had been some consideration of floating a bond issue to finance this project, but the receipt of revenue sharing funds has obviated this necessity.

Brattleboro, Vermont (population 12,239)
Person interviewed: Mr. Corwin S. Elwell, City Manager
Date of interview: February 2, 1973

Mr. Elwell explained that all towns in Vermont are required by a recent state law to change to a fiscal year accounting system (July 1-June 30) no later than July 1, 1977. Whenever the shift to this new system is made, it will be necessary for the

first budget to cover an 18 month period, January through June, plus the new fiscal year. Mr. Elwell sees revenue sharing as the perfect vehicle for Brattleboro to use in making the change-over. Therefore, the town has adopted a plan for making this change on July 1, 1973, and a budget has been submitted that will span the period January 1, 1973 - June 30, 1974. All the revenue sharing funds to be received by the city during this period will be used to cover the extra six months.

For the years of revenue sharing remaining after this budgetary shift has been completed, the town will probably use its funds for capital expenditures. It does not expect the program to become permanent.

Woodstock, Vermont (population 2,608)
Person interviewed: Mr. Sidney C. Smith, City Manager
Date of interview: February 2, 1973

Mr. Smith stated that the town of Woodstock plans to use all of its revenue sharing funds on capital expenditures, primarily a new fire station. Woodstock, like most towns, wants to avoid any new continuing programs in the event the revenue sharing program is not extended after five years.

The village of Woodstock, a separate governmental entity, but one with which Mr. Smith is familiar, plans to use about half of its funds for the reduction of property taxes. The town of Woodstock will use none of its funds for this purpose.

Concord, New Hampshire (population 30,022)
Person interviewed: Mrs. Marjorie B. Foote, City Clerk
Date of interview: February 2, 1973

Mrs. Foote explained that Concord is not getting as much money as originally expected. Like most other cities, Concord plans to use its money for nonrecurring expenses. This is to be accomplished by applying the money to the current budget to pay for capital expenditures already planned. There will be no new programs. Concord would definitely have had an increase in the property tax if revenue sharing funds had not been received. New Hampshire is the only state in the U.S. with no broad based source of revenue, except for a state lottery and some minor business taxes. It has neither a statewide sales tax nor a general income tax. As such, the cities in the state do not participate in the sharing of sales tax revenues as do many cities of states having this kind of tax.

Concord considers that revenue sharing has been of immense value to the city in allowing it to meet its obligations without a property tax increase.

East Hartford, Connecticut (population 57,583)
Person interviewed: Mayor Richard Blackstone
Date of interview: February 21, 1973

Surprisingly, Mr. Blackstone stated that East Hartford has no real need for revenue sharing funds. East Hartford is a city with a lot of heavy industry, and a substantial amount of revenue is derived from this source. The city has one of the lowest tax rates in the state, with a 65 percent level of evaluation

and a 42.5 millage rate. Even though it enjoys this low tax rate (low for Connecticut), East Hartford will use part of its revenue sharing funds for a tax reduction of 3-5 mills. There are no particular plans at the present time for the remainder of the money, but it will go for capital expenditures. A portion of it may be used for the purchase of police and fire department equipment. Until definite plans are made, the money will remain in an interest-bearing account.

New Haven, Connecticut (population 137,707)
Person interviewed: Mr. Everett Shaw, Director of the Planning and City Development Commission
Date of interview: February 21, 1973

New Haven is particularly worried about the possibility of cutbacks in other Federal programs. This interview was conducted at the time that much publicity was being drawn to the subject of revenue sharing as a means of effecting a reduction of grant-in-aid programs, etc. Mr. Shaw stated that revenue sharing funds are badly needed for New Haven to meet its responsibilities without a tax increase. The city already has one of the highest rates of taxation in the state.

Until the overall subject of Federal funding is clarified, the city is making no definite plans for the expenditure of funds. However, a decision will be necessary before the new fiscal year begins in July if a tax increase is to be avoided. Revenue sharing funds will definitely not be used for a tax cut.

Wethersfield, Connecticut (population 26,[illegible]62)
Person interviewed: Mr. Ralph Desantis, Town Manager
Date of interview: February 21, 1973

Mr. Desantis does not believe that revenue sharing deserves all the favorable publicity it has been receiving. He sees the whole program as an insidious plan to cut back Federal programs in other areas, with revenue sharing being used as a smokescreen. He also fears that the regulations applying to the revenue sharing program will grow.

Despite this pessimism (or perhaps realism), Mr. Desantis credits the present receipts for stabilizing the town's budget. Wethersfield has a high tax effort, one of the factors in the distribution formula, and as a result is receiving more money than most towns its size. The budget includes a relatively high level of capital expenditures, so revenue sharing funds will be directed toward this usage.

Hartford, Connecticut (population 158,017)
Person interviewed: Mr. Edward M. Curtin, City Manager
Date interviewed: February 21, 1973

Hartford is using part of its revenue sharing funds to improve the planning and managerial functions of the city government. This money will underwrite the cost of initiating a long-range financial planning unit which will monitor cash flows, establish investment schedules for the city treasurer, and perform long-range financial planning. An additional senior analyst will

be hired to study the cash-flow problems in an effort to relieve the internal audit staff. This program is obviously one of a continuing nature.

Some of the remaining funds will be used for capital expenditures, primarily equipment for the fire and police departments. A portion of the money will be used in various administration areas, particularly in the police department. At least half of the total revenue sharing funds will be used for programs that will require continuous funding. Hartford is giving particular emphasis to expanding and improving the police department and for upgrading the quality of city management. No revenue sharing funds will be applied toward a tax cut.

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Flannery, Donald. Chief Administration Officer, Granby, Connecticut, January 19, 1973.

Foote, Marjorie B. City Clerk, Concord, New Hampshire. February 2, 1973.

Hewitt, Sylvia. Public Relations Officer, Council of State Governments, Washington, D.C. January 17, 1973.

Keseker, Sarah S. City Clerk, Hartselle, Alabama. December 26, 1972.

LaCoe, Norm. Coordinator, Office of Federal Aid Programs, Alachua County, Florida. December 20, 1972.

Lloyd, Robert. Assistant to the Legislative Counsel, National League of Cities/U.S. Conference of Mayors, Washington, D.C. January 17, 1973.

Lopez, Antonio. City Finance Officer, Sante Fe, New Mexico. January 4, 1973.

Meyer; William. First Selectman, East Granby, Connecticut. January 19, 1973.

Moore, Thomas. Comptroller, Manchester, Connecticut. February 2, 1973.

O'Key, Clifford W. City Manager, Tucson, Arizona. January 2, 1973.

Olivi, Irma M. Town Clerk, Windsor Locks, Connecticut. January 19, 1973.

Palczynski, John J. Mayor of Westfield, Massachusetts. February 2, 1973.

Ritchott, Norman J. City Auditor, Chicopee, Massachusetts. February 2, 1973.

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Smith, Sidney C. City Manager, Woodstock, Vermont. February 2, 1973.

Sullivan, Daniel. First Selectman, Suffield, Connecticut. January 19, 1973.

Shaw, Everett. Director of the Planning and City Developemtn Commission, New Haven, Connecticut. February 21, 1973.

Desantis, Ralph. Town Manager, Wethersfield, Connecticut. February 21, 1973.

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Other

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C418 Cheshire
U.S. Federal Reserve
sharing: bluepring for
local tax relief or
increased tax burden?